

Audit Training and Capacity Building

Final Report

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Data Page

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- Compliance audit
- Compliance management
- Systems based audit
- Transaction based audit
- Client systems
- Internal controls
- Quality assurance
- Continuing professional development

Abstract

Specific Challenges to Be Addressed by this Consultancy

Jordan has made significant strides in customs modernization over the past few years. Despite this progress, there is still considerable work ahead for the Customs Department to transform itself into a modern organization based on international best practices. The Customs Department is responsible for ensuring compliance with Customs regulations, including the management of the operational interface with their respective agency partners in Jordan's civil service.

Audit is an important strategy in the overall approach to ensuring and improving compliance, and it needs to be done in a professional way and taking into account the sophisticated manner in which modern business is conducted.

This Scope of Work (SOW) is therefore designed to strengthen the audit capability of national customs. It is important to develop a capability that matches the standard of audit activity in the wider commercial world. In addition, it must be recognized that audit is an important strategy that allows for an effective balance between facilitation and control. It is an effective post-entry strategy for ensuring that business has met its obligations. If the business community realizes that the Customs Department employees are proficient and professional and targeted in their approach to audit activity, it sends a message to them that the potential benefits of being non-compliant are not worth the risk.

This SOW will ensure there is an effective audit methodology in place and it will promote an appropriate and effective relationship with the Intelligence, Legal and Enforcement Directorates of the Customs Department. Auditors may contribute to the overall body of knowledge held by Customs. They should also be effective in identifying and referring suspected fraudulent activity.

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EXECUTIVE SUMMARY

The principal objective of this consultancy was to develop a comprehensive compliance audit capability within Jordan Customs Department by providing skilled officers with a methodology and suitable processes and procedures. That objective has been achieved.

The Customs officers selected for training brought differing skills and experience to the classroom. Largely because of this, some of the principles and methods addressed were easier to comprehend for some than for others. I believe each person trained now has a basic and useable understanding of the principles and methods involved. Additionally, most also have a more advanced knowledge of a particular aspect of the work which can be harnessed to achieve group synergies.

Compliance auditing is not a strategy of itself. It is but one key element in a strategy to achieve continual improvement of levels of compliance with legislative or other requirements. The emphasis of a compliance improvement strategy is on ensuring future compliance rather than searching in detail for past errors. It is one of the aims of audit to examine internal company systems to ensure that a sufficiently strong control environment exists which will ensure the likelihood of future compliance subject to their being no major system changes.

This report concentrates on audit capability some aspects of the wider situation have become apparent and have been addressed.

A number of detailed recommendations are submitted in this report. The most significant of those are:

- That legislation be reviewed with the aim of enabling post entry audit of at least all relevant records but preferably to include the systems used to create and manipulate those records.
- That a specialized post entry audit section be established.
- That Customs field audit activity be limited to (a) evaluation of clients wishing to enter a partnership arrangement with Customs, (b) identified targets of a risk management system and (c) randomly selected clients / events to validate the risk management system.
- That quality assurance testing of completed audits be initiated

INTRODUCTION

The principal objective of this consultancy was to develop a comprehensive compliance audit capability within Jordan Customs Department by providing skilled officers with a methodology and suitable processes and procedures.

Compliance auditing is not a strategy within itself. It is a key element in a strategy to achieve continual improvement of levels of compliance with legislative or other requirements. Such a strategy would include the following elements:

- responsible and informed self-assessment;
- a partnership approach with industry;
- client education and service;
- appropriate development and support for Customs staff;
- clear legislative and administrative requirements;
- a risk managed, coordinated approach;
- **appropriate audit activity;**
- an appropriate penalty regime; and
- quality assurance.

The emphasis of compliance improvement is on ensuring future compliance rather than searching in detail for past errors. It is one of the aims of audit to examine internal company systems to ensure that a sufficiently strong control environment exists which will ensure the likelihood of future compliance subject to their being no major system changes.

It is in environment of a compliance improvement strategy that some of the recommendations in this report are made. While the report concentrates on audit capability some aspects of the wider situation have become apparent and have been addressed.

SPECIFIC TASKS OF THIS CONSULTANCY

Task 1

Review the existing audit methodology and make recommendations for improvements that are consistent with international best practice and the audit process (e.g. systems based audit).

Review

I have had limited access (due to time) to existing Customs practices but it appears that audits are generally limited to desk audits and field enforcement inquiries. There is no apparent history of post entry field audit, either transaction or systems based.

I make the assumption, again based on limited observation, that the Customs Department in Jordan is intent on improving cargo facilitation, gaining confidence that monies due are paid in a timely manner, ensuring compliance with relevant legislation, and minimizing administration costs – i.e. implementing a compliance management strategy.

A process intrinsic to achievement of such objectives is that of change management. Attitudinal change in Customs will be essential and is likely to be challenging. A reasonably rapid change will be needed to engender the trust of Customs' clients.

Self assessment does not appear to be available at any level which significantly impacts on the client. Original commercial documents must be lodged with the Customs Declaration and decisions as to processing treatment are exclusively by the regulating authority. Further, my understanding of the system is that even importations which are 'green lined' will receive an 'amber' level check if the staff resources are available (this is contrary to the 'official' line but it seems to be the actual position). This cultural position must mitigate against Customs' ability to manage trade growth within existing staff numbers.

On the basis that self assessment with lodgment of supporting documentation only when required is not yet viable, it would seem preferable to retain only copies of the commercial documents (using scanning, microfiche or microfilm technologies). Original documents are not currently available to audit at a client's premises but must be sourced from Customs records. Additionally, the client's ability to implement internal controls on their importation process is limited if not denied.

Post entry audits (systems or transaction based) are viable when:

- Legislation enabling post entry review of client records is in place; or
- The clients volunteers access to its systems and records, presumably in exchange for a particular benefit; and
- Client systems are able to be documented

A systems based audit is only viable when:

- Legislation enabling post entry review of client systems and records is in place; or
- The clients volunteers access to its systems and records, presumably in exchange for a particular benefit; and
- The client is not a sole operator; and
- Client systems are able to be documented and are comprehensive; and
- Adequate internal controls are in place or the client is willing to introduce and maintain such controls.

Task 2

Design a compliance audit course, taking into account the skills and experience of Customs Department officers and existing customs related legislation, policy and procedures.

Output

I modified a basic compliance audit course to maximize the limited time available and with regard to existing customs legislation, policy and procedures. During the twelve days allocated to training the participants would be available for a maximum of fifty (50) hours. Variations were introduced to compensate for the large number of participants – there were thirteen (13) compared to an ideal class size of eight (8) which allows for more direct instruction and review.

The presentation of the course was modified as necessary throughout to maximize its usefulness to the participants with their existing skills and experience.

Of particular benefit to the course design was the availability of a Jordanian importer which had volunteered access to its systems and documents for training purposes. That company was The Far East Equipment Co and its assistance warrants recognition.

The training and reference materials provided to participants and referred to at Appendix D were created prior to this consultancy and not for this task specifically.

A timetable was distributed – Appendix E1.

Task 3

Deliver the training course on compliance audit to selected officers of Customs

Output

The original timetable for the course is at Appendix E1. The intent was always to be flexible to suit the needs of the participants. A revised timetable (Appendix E2) was distributed in the second week.

Training was delivered in accordance with the revised timetable. Timings and time allocated were at the request of Mr. Mahmoud Wafa, Director Risk Management, and with the concurrence of Mr. Walter Hekala, CRM Manager PSPI, AMIR Program.

Attendance. Eleven (11) of the thirteen (13) participants attended all sessions. One officer missed two sessions, another missed three sessions, both due to operational priorities. They made up the shortfall through discussion with other participants, out of class study, and some additional tuition. In my judgment these two officers were within the most capable and committed group on the course. The situation was discussed with the director of the Risk Management Directorate and the AMIR Program's Customs Reform and Modernization Subcomponent manager.

Participation. All participants contributed actively in both classroom and field audit sessions. Discussion periods were lively and a significant aid to skill and knowledge transference.

Language issues. I was assisted in most sessions by a very able interpreter. While the use of an interpreter necessarily limits the volume of material delivered, I am confident that the participants understood the principles and methods discussed and demonstrated.

Facilities. The training room provided for all but one session was excellent. The room itself was of a good size for the numbers involved and the training aids were very good. The assistance provided by support staff was excellent and had a significant impact on the success of the training.

Use of a 'live' training exercise at a client's premises. Visits to the client were programmed so as to enable actual situations, systems and records to be used as training aids during classroom sessions. This worked exceedingly well as it illustrated clearly the work involved and contributed to the participants' confidence in the skills they had learned.

Outcome

Participant evaluations. Each participant was asked to complete a standardized evaluation form. In summary, the participants reported that:

	Materials	Trainer	Practical Application	Venue	Overall Rating	Translation
Excellent	6	8	6	11	11	8
Good	7	4	6	1	5	5
Fair			1	1	1	
Poor		1				

Topic	Most Useful	Least Useful
All	3	
None		1
Field visits	5	
Flow charting	6	1
Sampling	2	2
Reporting		1
Internal controls		2
Audit methodology	1	
Systems analysis	2	
Types of audit		1
CAPE matrix	1	
Working papers		1

Would you recommend the training to others: 12/13

How could this training be improved. The recurring theme is to extend the period of training to allow for more practical training in the field. Some would prefer less theory.

My evaluation: Overall, I believe the course has been extremely successful in meeting the prime objective of this consultancy.

All of the graduates now have the basic skills needed to conduct compliance audits. Importantly, I believe they all also now have the necessary confidence in their own abilities.

Customs' client base does not appear to include many, if any, large companies with particularly complex internal systems. Providing that the graduates have the opportunity to use their new skills regularly, can develop team synergies, and have access to continuing professional development they should become highly effective in their environment over time.

Task 4

Advise on the implementation of the Strategic Audit Plan including recommendations on issues such as post entry audit, organizational structure (e.g. business units), audit process (e.g. systems based audit), and the application of a risk managed approach.

I have examined the Strategic Audit Plan and discussed many of the recommendations with Customs and AMIR Program staff. I have also reviewed some of the current practices with operational Customs staff, other AMIR consultants and management at The Far East Equipment Company. The Far East Equipment Company is the one which volunteered access to its systems, records and staff for training purposes.

My recommendations are grouped with those resulting from other specific tasks.

RECOMMENDATIONS

1. That legislation be reviewed with the aim of enabling post entry audit of at least all relevant records but preferably to include the systems used to create and manipulate those records. A time limit of five (5) years would be reasonable.
2. That self assessment by informed importers be examined as a means of transferring both responsibility and workload from Customs to the client.
 - i. That action is taken to ensure that the clients who interact with Customs are fully informed. As an example of one way in which other administrations address this issue is a publication by the Australian Tax Office (appendix G) which is sent to all clients prior to audit (with a letter giving notice of the audit).
3. That the retention of original commercial documents by Customs be discontinued so that importers are able to assume full responsibility for their systems which create Customs Declarations. It would also reduce security and storage implications for Customs.
4. That a specialized post entry audit section be established.
 - i. That the post entry audit section be responsible for all post entry audits for Customs whether systems or transaction based.
 - ii. That systems based audit methodology is employed whenever appropriate.
 - iii. That a formal continuous professional development (CPD) program within the section be established.
 - iv. That initially the ratio of auditors per supervisor / manager is no more than 10:1. Should quality audit management software be introduced in the future a ratio of 16:1 would be reasonable.
 - v. That a culture of continuous improvement be fostered in the unit.
 - vi. That a small number of 'trainee' or 'apprentice' positions be created within the group as a means of developing new members for the unit.
 - vii. That it be accepted that twelve months is a reasonable minimum time in which to expect a new member to become fully effective when adequate CPD is available.
 - viii. That involuntary rotation of the most skilled operatives is avoided where possible due to the high and ongoing organizational and personal training costs.
5. That compliance levels in each area of activity be bench-marked to establish the initial position.
6. That Customs field audit activity be limited to (a) evaluation of clients wishing to enter a partnership arrangement with Customs such as the Jordan National

Customs “Golden List” program, (b) identified targets of a risk management system and (c) randomly selected clients / events to validate the risk management system. To effectively operate in a trade-supportive environment the following principles for audit notification are applied:

- i. Clients are advised in writing at least thirty (30) days in advance of the intention to audit. The advice should contain the scope of the audit planned and information as to both Customs and the client’s rights and responsibilities.
 - ii. ‘Audits without notice’ be extremely limited in number, precise in scope, and requiring that the situation be put, in writing, to senior management. The written approval of senior management should be a requirement as this is a situation where operational priorities are over-riding compliance policy.
7. That quality assurance testing of completed audits be initiated approximately six (6) months after the first audit is completed.
 - i. That testing includes measures of both outputs and outcomes.
 - ii. That, while recorded and reported on, the primary aims of this testing be to foster continuous improvement and recognition of excellence.
 - iii. That the accountability of the results be enhanced by the inclusion on the evaluation panel of a person external to the Customs Department – for example a suitably qualified academic or a member of a national body representing auditors.

Appendix A

Documents Read During the Course of the Consultancy

- AMIR Technical proposal
- AMIR 1.0 Final Report
- Customs Department Strategic Plan: 2001-2003
- Development and Integration of Customs Reform and Modernization within Jordan 2002 Final Report, February 2003. Prepared for AMIR Program by Glenn Wood.
- Development of Border Risk Management, Intelligence & Risk Management Capabilities Final Report, January 2003. Prepared for AMIR Program by John Knott, John Howard and Michael Krstic.
- Import process maps prepared for AMIR by John Howard 2004
- ASYCUDA descriptive material
- Customs Department Draft Strategic Plan 2004-

Appendix B
Individuals Interviewed During the Course of the Consultancy

NAME	TITLE	ORGANISATION
Walter Hekala	CRM Manager, PSPI	AMIR Program
Greta Boye	PSPI Team Leader	AMIR Program
Jamal Olaimat	Customs Specialist, PSPI	AMIR Program
Lina Arafat	Customs Projects Liaison, PSPI	AMIR Program
Rand Hannun	Consultant (Legal)	AMIR Program
Bashar Rashdan	Consultant (Legal)	AMIR Program
John Howard	Consultant	AMIR Program
Andrew Ford	Consultant	AMIR Program
Rami Khyami	Training & Events Coordinator	AMIR Program
Sulaf Mubaideen	Public Relations Specialist	AMIR Program
Diane Scott	Communications Manager	AMIR Program
Jan Tomczyk	Consultant	AMIR Program
Mahmoud Wafa	Director Risk Management	Jordan Customs
Marawan Ghrabieh	Director Planning & Organization	Jordan Customs
Wadie Z. Ibrahim	Managing Director	The Far East Equipment Co.
Zeid W. Ibrahim	Assist. General Manager	The Far East Equipment Co.
Maher Abu Hweij	Shipping Dept.	The Far East Equipment Co.
Darwish A. Jammal	Parts Dept. Manager	The Far East Equipment Co.

Appendix C
Individuals Who Attended the Training Event

NAME	SECTION
Abdallah Abu Braik	Head Auditing & Control Section
Khaldoun Al-Sakit	Internal Audit Directorate
Abelrahman Al-Smadi	Risk Management Directorate
Mohammad Joudeh	Valuation Directorate
Imad Al-Dabbas	Tariff Directorate
Amin Khasawneh	Risk Management Directorate
Anas Al-Sh'er	Risk Management Directorate
Malik Afaneh	Risk Management Directorate
Aiman Al-Shneik	Risk Management Directorate
Mohammad Shbeilat	Amman Customs House Center
Moh'd Abu-Ta'a	Zarqa Free Zone Customs House Center
Badee' Shamout	Queen Alia Airport/Cargo Customs House Center
Samir Al-Safadi	Planning & Organization Directorate

Appendix D
Handouts and Training Materials Distributed During the Training
Event

Appendix D1. Course reference notes in bound form.

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- Section 1: Audit as a Compliance Strategy
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- Sub-section 1/2: Standards for auditing
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- Sub-section 1/4: Using the methodology
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- Section 2: Flow-charting
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- Sub-section 2/2: Basic principles of flow-charting
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- Section 3: Sampling
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- Section 4: Audit Methodology
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- Sub-section 8/7: Audit Report
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- Sub-section 8/8: Folder Of Attachments
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Audit as a Compliance Strategy

The role of audit in Compliance

Compliance strategy recognises that audit is only one means of addressing risk. An audit is an evaluation of company practices and records to assist in forming a judgement about the integrity of information supplied under self-assessment arrangements. In addition, audit will also serve to find and recommend ways in which the client can improve their compliance.

The role of audit will be focussed more on obtaining agreement with each entity on a level of internal control which is mutually accepted as being adequate to provide a high level of assurance that:

- revenue owing is received at the point that it falls due; and
- compliance with legislative requirements in relation to the production, storage, usage/movement/sale of products and retention of adequate records.
- Evaluation of systems and procedures
- Compliance strategy also seeks to change the focus of audit activity from the verification of individual transactions, to the examination of the internal controls over the client's systems and the procedures responsible for producing those transactions.

In an environment of self-assessment and an ever-increasing number of commercial transactions between industry and Customs / Revenue authorities, a systems based audit technique is used. This involves testing of the internal controls along with an appropriate number of transactions and gives a greater assurance about the likelihood of future compliance than the testing of transactions alone. However, there are still situations and certain types of operations that will not be suited to a systems based approach, and in these cases auditors will revert to a transaction-based audit.

The methodology

The audit methodology for use by the compliance teams is known as the *Audit Methodology*. This is a systems based approach (**SBA**). Where SBA is not appropriate, a transaction-based approach (substantive testing only) is adopted.

Whilst management decides on whether an audit will be comprehensive or focussed, it is the auditor who must make a decision, after an initial assessment of the controls in place, whether the client is suitable for a systems based audit approach or a transaction based one.

As an example, a comprehensive audit of a large company would cover all aspects of its relationship with Customs / Revenue. A focussed audit may examine one aspect of the companies operations. Whether a systems based or transaction based approach is suitable in the circumstances can only be decided after an assessment has been made of the internal controls in relation to activities. Audit Methodology is covered in detail in these notes.

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Current audit powers

Audit powers are country / agency specific and are not covered in these notes.
Standards for auditing

Integrity, objectivity and independence

Auditors shall be straightforward, honest and sincere in their approach to their professional work. They must be fair and must not allow prejudice or bias to override their objectivity. They shall maintain an impartial attitude and both be, and appear to be, free of any interest which might be regarded, whatever its actual effect, as being incompatible with integrity and objectivity.

Confidentiality

Auditors shall respect the confidentiality of information acquired in the course of the audit and shall not disclose any such information to a third party. In the case of release of information to other government agencies, the relevant authority should be obtained under the appropriate legislation prior to release.

For those clients who are concerned about forwarding commercially sensitive information to the audit team (and where there is no legislative onus on the client to do so) the Compliance Team Manager may consider drafting a 'Confidentiality Letter', if the information sought would help with an assessment of compliance.

Any consultancy people from outside of the regulating authority hired for their expertise in a certain field to give assistance to the audit team are also bound by this confidentiality. If those people are themselves members of a professional association then they may be additionally bound in terms of confidentiality by their own associations' ethical guidelines.

Skills and competence

The audit shall be performed and the report prepared with due professional care by persons who have adequate training, experience and competence in auditing. The Compliance Team Manager shall take care in selecting the composition of the audit team. If immediate human resources do not have the specific knowledge or skills required to deal with the scope and objectives of the proposed audit (eg knowledge of functionalities, commodities, IT, etc), then the Compliance Team Manager shall source that expertise from outside their group.

Work performed by assistants

When auditors delegate work to assistants, they shall carefully direct, supervise and review the work delegated. The Compliance Team Manager will endorse working papers progressively as part of the audit quality assurance program.

Work performed by other auditors and experts

When auditors use the work performed by other auditors or experts (eg previously conducted audits by Customs / Revenue, external audit under prudential arrangements, or evaluation by the company's own internal audit section) they continue to be responsible for forming and expressing an opinion on compliance.

The audit team shall obtain reasonable assurance that the work performed by other auditors or experts is adequate for their purposes.

Documentation

Auditors shall document matters that are important in providing evidence that the audit was carried out in accordance with Auditing Standards.

Working papers that meet the relevant Auditing Standards are incorporated in the Audit Methodology found in this Manual.

Planning

Auditors shall plan their work to enable them to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client's business and shall be further developed and revised as necessary during the course of the audit.

Audit evidence

Auditors shall obtain sufficient appropriate audit evidence through the performance of compliance and substantive procedures to enable them to draw reasonable conclusions on which to base their opinion on compliance.

Internal control structure

Auditors shall gain an understanding of the internal control structure of the client. If suited to a systems based audit approach, the audit team shall study and evaluate the operation of the internal control structure or elements thereof upon which they wish to rely in determining the nature, timing and extent of other audit procedures.

Audit conclusions and reporting

The auditor shall review and assess the conclusions drawn from the audit evidence obtained as the basis for expressing the audit opinion on compliance. This review and assessment involves forming an overall conclusion as to whether, in material respects, the client is complying.

The audit report shall clearly state the audit team's assessment of the client.

Audit Objectives

The objectives of a Compliance audit are:

- to assess the level of the company's compliance with requirements;
- to assess the adequacy/effectiveness of the company's internal control structure in respect of Compliance; and
- where necessary, to help improve the company's future Compliance by recommending appropriate changes to their systems.

Nature of audit activity

A systems based audit is desirable as this is necessary to form an opinion as to the effectiveness of the company's internal controls to ensure ongoing legislative compliance as well as timeliness, completeness and accuracy of payments made to Customs / Revenue.

Compliance and substantive testing will be aimed at establishing this opinion and verifying the integrity of the company's systems with respect to those payments over the audit period and to also establish a basis for future monitoring.

In the compliance environment, audits should be seen as an opportunity to assist industry and clients with improving compliance. Assistance in overcoming deficiencies, providing recommendations on methods to improve compliance and suggesting enhancements which make current compliance practices more effective are all positive aspects of an audit. The audit should also be seen as an opportunity for clients and industry to meet and discuss issues with audit staff.

As well as advising the company of the outcome and issues arising from an audit, a compliance report on issues that may need to be addressed internally is also seen as an important audit outcome.

Frequency of audit activity

Unless ongoing monitoring detects anomalies or unexpected variances, under normal circumstances a company may not be audited again for several years. The timing of future audits may be influenced by such factors as: the outcome of the company audit; notification of major changes to the company's technology, systems or procedures; results of monitoring or analytical review and other industry intelligence obtained.

Using the methodology

Suitability for Systems Based Auditing

It is envisaged that most companies will have some systems and procedures in place for the handling of Customs / Revenue related business. Consequently, the audit team will initially plan the audit using a systems based approach. However, there will be certain circumstances, principally where internal controls do not exist or are ineffective, where the compliance-testing phase of the process should not be applied.

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For example, compliance testing would be inappropriate in the following circumstances:

- companies that have a very limited number of transactions with Customs / Revenue and any sample for testing purposes would equate to the entire population of transactions;
- companies in which the person/s responsible for the preparation of Customs / Revenue related business transactions also have a vested financial interest in the company and as such no reliance can be placed on any system or designated internal control;
- where the audit team has no confidence in the reliability of internal controls. For example, stock-takes performed by one person, stock-takes performed by persons working with the stock, checks performed by poorly trained staff, etc; and
- where the client has refused permission for the audit team to examine the relevant systems.

Approach for companies not suitable for Systems Based Audit

In the case of a company not being suited to a systems based audit, the audit team leader shall seek approval from the Compliance Team Manager not to proceed with that approach with the reasons for this conclusion documented appropriately. The audit team will need to consider alternate audit techniques, generally some form of appropriate substantive testing of transactions.

Flow-charting

Definition of a flow-chart

A flow-chart is a diagrammatic representation which traces the flow of products, documents or data through a system. It has the following features:

- specifies the sections or activities covered;
- uses standard symbols to represent documents and records; and
- uses flow lines in a standard way to show what, when and how things happen.

Why flow-chart

To describe a complex process, a well drawn flow-chart is simpler than a narrative to read and understand because it can:

simplify complex operations. The ‘pictorial’ view quickly conveys a number of complex interactions together better than a narrative can;

be easily amended. When systems change a new amended version can be created either by altering it (if drawn in pencil) or by printing a new version from the charts stored in the computer library;

show how systems fit together. It is useful to show how all the systems within a company operate and combine because it is much harder to ‘lose’ goods or information when it is drawn and it cannot just disappear off the page; and

allow detailed analysis. An overview of a licensee's operations is a good starting point for assessing the effectiveness of internal controls. They are often used in our audits to record information gathered in the field and to reduce time spent in research by the next auditor. Despite these advantages flow-charting is still just a tool to achieve audit objectives, not an end in itself, and may not be the best choice in every case.

When to flow-chart

Not all systems are represented best by a flow-chart. Small systems are more clearly described by a brief narrative except when done as a training exercise, however, as processes become more complex wherever possible try to show information with a flow-chart.

Not all information can be shown easily on a flow-chart and narratives should be used to supply additional information to add to the understanding of the system. In each case, you must decide whether footnotes or a narrative best suit the situation.

Basic principles of flow-charting.

There are several basic principles that should be applied to every flow-chart. These are:

- plan ahead** and use drafts to keep the flow-chart clear and easy to understand;
- prepare overviews and drafts** to organise the overall layout before spending time adding details;
- label every chart** to clearly identify the licensee and the systems described;
- include the names** of the author and reviewing officer (usually the audit supervisor) and **the date** when the chart was made in the header and update these details for any later amendments that are made;
- use footnotes** if necessary to explain activities in more detail but clearly number them;
- use abbreviations** to keep the chart uncluttered but explain in full any abbreviations used in a legend somewhere on the flow-chart; and
- use several** less complex charts and an overview chart rather than a single chart with too much information on it.

Extra principles of Customs / Revenue flow-charting

Customs / Revenue uses a flow-charting technique called '**horizontal charting**'. In this technique processes or document movements have a horizontal flow from left to right across the page between various sections, positions or activities as shown on Section 5/3. The layout should be pre-planned to:

- keep flow-lines as short as possible;
- avoid long meandering lines; and
- flow-lines should never cross.

Note: **Crossed and long meandering flow-lines add confusion and are difficult to follow. They make a flow-chart appear more complicated than it really is.**

Separating sections of the flow-chart

Usually, the names of the sections or individual positions, which perform specific functions, are placed in a row of headings across the top of the page, separated by short vertical lines. Each section in the process then has a designated flow-chart area which is the width of the spacing allocated to its name. This space extends all the way down the page. This is always done in documentary flow-charting and is preferable, but not always done in process flow-charting.

It is important to bear in mind the relevance of the information you have gathered to your reason for flow-charting. It is usually necessary to find the right balance between having too much extraneous detail or not enough of the needed information. The objectives of the job must be satisfied while keeping the flow-chart as simple as possible by eliminating any irrelevant information.

Basic flow-charting conventions

Process flow-charts

Before going on to strictly defined symbols and styles for **documentary flow-charting** in module three, this module will look at **process flow-charts**. These charts describe the physical movement or transformation of goods.

The symbols used in process flow-charting may be simple 'boxes' labelled with each processes or by using more pictorial symbols such as trucks, factories, etc. The choice of symbol is flexible, unlike documentary flow-charting, where the correct standard symbols must always be used.

Flow-lines are used in process flow-charting to show the sequence of processes or the physical movement of product from one operation/ treatment to another. The same basic rules apply to the creation of both process and documentary flow-charts:

Direction of movement

In a flow-chart the overall direction of movement is from the top left-hand corner, to the bottom right-hand corner. In very simple flow-charts this can be easily done but once flow-charts become more detailed, it is necessary to vary the direction of flow in the later parts of the flow-chart in order to obtain the clearest possible layout.

This can include:

starting lower on the left-hand side to allow a later process to be brought in from above the initial flow.

backtracking within a particular area of the flow-chart to fit in all the processes, or backtracking across the flow-chart to show products or documents returning to the area they originated from.

The only limitation to this flexibility is that flow-lines should **never** cross and that diagonal flow-lines are used only in special circumstances (such as using a fork in a flow line to indicate alternative possibilities).

Points to note

The basic flow is left to right and up to down; however this is varied where it is felt this more easily depicts the process: for example, the right-to-left flows in the Product section.

Although dividing the chart into quarters shows areas of operation, rather than the page-height columns used in Customs / Revenue method, the advantages of dividing the chart to illustrate the distinct areas of operation are clear.

Start arrows are used to depict the beginning of each process or the sequence of entry of product or documents into the system. These are numbered in order of occurrence. The first start arrow generally appears in the top left hand corner but this can be varied if needed to arrange the flow-chart in a clear fashion later arrows can occur anywhere on the page as each process begins.

In process flow-charting, it will often be found necessary to show additives to the main product. The preferred methods of doing this are either, a footnote or a labelled arrow joining the process.

Rough drafts

Your first attempt at a flow-chart should be a rough draft. It need not meet all of the requirements of the final product because the aim is just to 'get it all down' so that you can look for errors or sections of the process that you have not yet covered. It can sometimes require several attempts to organise the chart before you have the clearest layout and it is sometimes a good idea rather than trying to 'reinvent the wheel' to look for a similar flow-chart already drawn for another company in the same trade. It is often surprising how similar procedures are from company to company.

Subdividing the flow-chart

The top of each chart must be divided into areas of activity or responsibility. The division of the chart into company sections, or responsible personnel, is an essential guide to where documents move and action occurs. The divisions extend down the full length of the page although the dividing lines need not.

The decision whether to divide the chart by sections, by positions, or by activities, and the number of divisions in the heading, depends on the judgement of the officer preparing the flow-chart. It is often based on the division of duties from an internal control point of view. It will depend on the size of the company and whether functions are performed by individuals (eg warehouse manager) or sections (eg Dispatch).

The division of the chart into areas clearly shows the physical location of separate processes. This is a simple left-to-right flow. Charts that are more complex may require you to experiment with several arrangements of headings during drafting, to determine which arrangement gives the clearest layout.

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Some points to note:

the beginning of a process is indicated by a start arrow;
either labelled boxes or elaborate symbols can be used to depict processes;
solid lines and arrows show direction;
solid lines and arrows show the direction of movement between processes;
forked flow line (diagonals) show alternative possibilities;
no directional arrows are necessary to show documents, goods, etc leaving the system;
explanatory notes and product descriptions can be placed within the flow-chart.
Footnotes can also be used if the author feels they would result in a clearer chart;
however this can sometimes be quite distracting when there are many small notes.

Basic documentary flow-charting

Main difference to process flow-charting

Documentary flow-charts show the physical movement of 'pieces of paper' within the company and the movement of information among documents (eg recording details from one document onto another).

The Customs / Revenue standard

Documentary flow-charting establishes a **common language** of symbols and meanings by using **standard symbols** to identify the type of document and what happens to it. The flow-chart records your knowledge of the company's operations in a form which any other person familiar with flow-charting can understand. This eliminates ambiguity and omissions which can occur in a narrative written by someone who already understands the system but read by a novice.

For this reason, Customs / Revenue standard symbols must be used on every chart

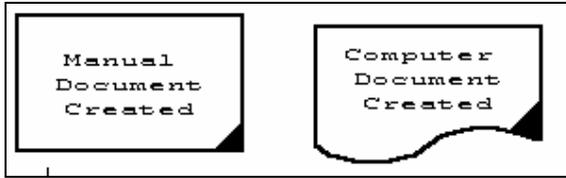
prepared for Customs / Revenue.

Standard symbols

The standard symbols for documentary flow-charting and their use is now discussed one step at a time.

Start points: The beginning of each new process, or the entry of a document from outside the system, are indicated by start arrows numbered in the order in which they occur. The first start arrow is usually shown on the left-hand side of the page and the flow-chart drawn so that it reads from left to right across the page. However, when there are several inter-related starting points, common sense should be applied in their positioning, keeping clarity as the key objective.

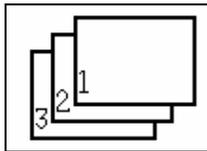
Documents: A number of types of documents will be encountered at a typical premise and a distinction is made between manually produced and computer-generated documents.



If a document does not enter a system at a start point, it must be created within the system. These documents do not have start arrows. Putting a dark triangle in the bottom right-hand corner signifies the creation or preparation of documents. When a number of copies are created this is shown by actually drawing the number of copies into the flow-chart.

When multiple copies of one document are created, it is common to see flow-charts showing the 'created' symbol on the top copy of the set only. While this is not incorrect, it is recommended that all newly created copies are marked, as this gives a much clearer result in complex flow-charts where many documents are involved.

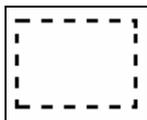
If documents are part of a pre-numbered series, a note to this effect should be included when they are created. Multiple copy documents should be numbered to indicate first, second, etc copies, or lettered ((w)hite, (y)ellow, etc) where different coloured copies are involved. Being able to identify which copies undergo which processes can be crucial to understanding the workings of a system.



Note that during the drafting of the flow-chart it may be necessary to experiment with the order in which the set is shown to allow a smooth flow later in the chart.

A document shown in dotted outline indicates that it only occurs in special circumstances; a note should be included to indicate what these circumstances are, if it is not clear from the context.

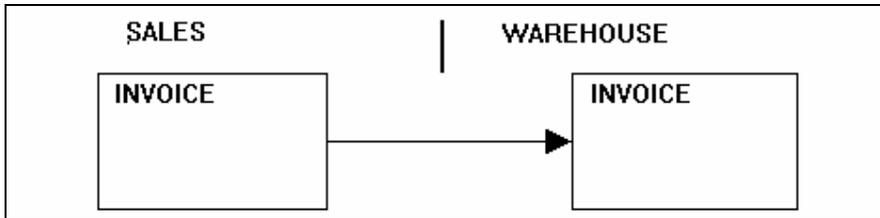
All documents should be named. If abbreviations are used a legend or key to abbreviations should be included in the flow-chart.



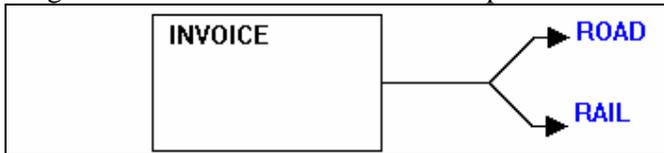
Documents should be reproduced (shown again) after they move to a new area and as a set after joining. The only exception would be within a very complicated chart where space precludes this and the meaning is still clear at a glance.

Flow-lines

Solid flow-lines show the movement of a document from its source, to its ultimate filing, departure outside the system or destruction.

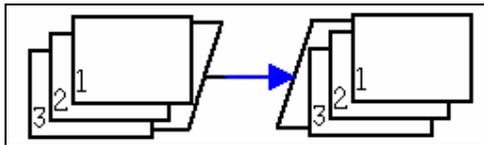


Diagonal flow-lines indicate alternative possibilities.



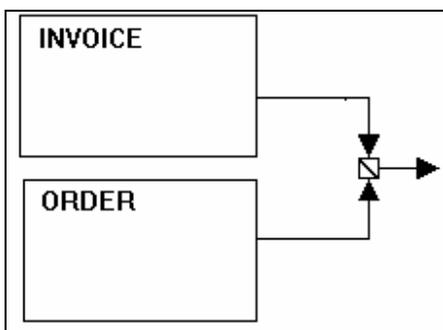
Sets: Brackets are not required on the left side of a set of documents when they first enter the system or are created; but they are required after that whenever the documents move as a set.

Because of the general left-to-right flow of Customs / Revenue charts, the preferred slope for a set of documents is as shown below.

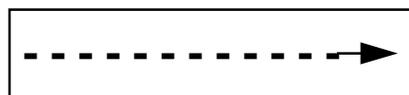


It is conventional to enclose sets in brackets which follow the slope of the set (however, if the Flodraw or ABC Flowcharter software is used, it will be found to be faster and more presentable to use vertical brackets by drawing lines without arrows on the end). The choice is up to the flow-charter's discretion; however, for the sake of presentation, use only one type of bracket in any one flow-chart to be consistent.

The **attaching symbol** is used to show when documents are combined into a set. The documents should be shown together as a set, after attaching, before any further processes are shown.



Information flow: Dashed flow-lines with arrowheads to show the direction of movement. They show the movement of information ONLY between documents.



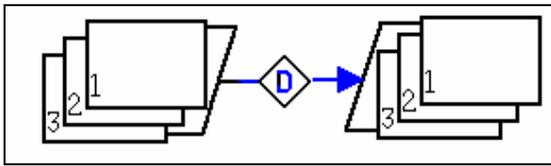
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A one way arrow a one way flow of information (such as typing information into a computer) while a two-way arrow indicates either the recording of information from each document onto the other or the comparison of some information (an example of this is a telephone call where both people on the line gain information).

A note should be added to show what information is recorded or compared, where it is not clear from the context of the flow-chart alone.

Temporary and Permanent Files

The diamond symbol is used whenever a document is held in a location waiting for a particular event to occur. It is described as a file although it may physically take the form of a clipboard or a tray on someone's desk. The order of filing is indicated by placing a letter A, N, or D (for alphabetically, numerically or by date) within the file symbol.



A note should be included to indicate the event that causes the document's removal from the temporary file. Documents should be reproduced after removal from a temporary file.

The only exception to this is where they leave the temporary file directly to a destroyed box (a black square) with no further action in between.

Ultimate Fate of a Document

All documents shown in the flow-chart must eventually move to:

a permanent file;

a 'leaves system' symbol;

an off-page connector (moves to a system on another chart), or

the destroyed symbol.

(This is a useful hint when flow-charting in the field as it provides an easy check as to whether you have discovered everything that happens.)

Note that directional arrows are not used when showing movement to a permanent file, destruction, or leaving the system.

Permanent file

Eventually all information and documents must be stored, destroyed or leaves the system being audited.



A flow line may terminate in the triangular 'permanent file' symbol, from any direction. As with a temporary file the order of filing is indicated by placing a letter A, N, or D (for alphabetically, numerically or by date) within the file symbol. This can assist future auditors to locate documents during checks.

Destruction

The destruction symbol is a black square. No arrows are used to the destruction symbol.

Leaving the system

The point at which a document leaves the system is dependent on what the flow-chart considers part of the system being recorded. For example, a document may leave the system 'To Accounts Section'; in another flow-chart, the workings of the accounts section may be considered relevant enough to be included as part of the flow-chart. The symbol is like a capital



Some documents may leave the system and re-enter the system later at a new Start Point.

Off-page connectors

Flow-charts for large companies may consist of several pages; or a document may move from one system to another.



The Off-Page Connector symbol is used to indicate that a document leaves the chart, to reappear on the page number indicated in the symbol. Its' reappearance on the other page is marked with a start point and the Off-Page Connector symbol indicating which page it came from.

Registers and logbooks

These are typically permanent records for consecutive entries, such as dip books or shipping registers. In contrast to documents, registers may 'float' around a flow-chart and be shown anywhere, in whichever section the action occurs. A note may need to be included in the chart to indicate the register's normal storage location.



When information is recorded in a register from another document, a note or footnote adjacent to the information flow line indicates which details are recorded. It is common to encounter situations where the information originates from a physical source such as a dip, temperature or time reading. In this case, there will be no information flow line, and a note or footnote adjacent to the register itself is sufficient to describe the data recorded.

Initialed, signed and endorsed symbols



The 'signed', 'initialled' and 'endorsed' symbols may be used on a register if desired; however, this is optional. Notes are more usually used to indicate what is recorded in a register.

These are used on documents to indicate where a signature, initials or certain information is routinely added to a type of document. Where there are multiple copies, the placement of the symbols (or a note) should indicate which copies have been signed.

If it is not clear from the context who signs or initials the document, this should be indicated by a note. Any action on which the signature, etc depends (eg a physical check) should be indicated.

Finalising a flow-chart

On completion of a flow-chart in the field, it will be necessary to 'walk through' the system with company staff to ensure that things really do occur as per the flow-chart. This is the final step in flow-charting a real system.

Further documentary flow-charting **Relevance of flow-charts to systems theory**

Flow-charts are drawn to help you and future auditors to understand the basic concepts of the systems used in a company and to assist in the problem-solving processes for the more complex documentary systems that exist in larger businesses. By including this information, a properly constructed flow-chart can contribute significantly to understanding a system and how the whole company operates.

Some flow-charting problems **Defining the system**

When flow-charting in the field the auditor must decide where the flow-chart will begin and end. Systems encountered during an audit will have inputs and outputs that are not clearly isolated from their external environment.

This should be done in a logical manner, keeping in mind the reason for flow-charting and the extent of Customs / Revenue interest in the company's operations.

For example, when preparing flow-charts for a whole company, flow-charts could be prepared for a 'Receipts' and a 'Dispatch' system; or (in a small company) simply for 'Stock Control'. In one company, these functions may be carried out by separate staff in physically distinct receipts/dispatch offices; in another office, by one person.

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Consequently, the start points and exits from a flow-chart, where it interacts with the outside world, will depend on the auditor's judgement, based on his/her knowledge of the company, and of the areas of interest to Customs / Revenue. For example it would be reasonable to ignore the staff pay system.

Page divisions within systems

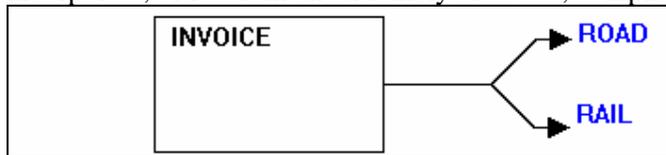
When a system is large, it will require more than one page to each chart. The division should be made so the amount of inter-chart cross-referencing (documents flowing from one chart to another) is minimised.

Where a number of systems in the set of flow-charts fit in together, it may prove useful to construct an overview flow-chart, showing the relationships among the systems. This can enhance understanding of the company's full operations and act as a guide through the detailed charts.

Depicting alternative actions

Three methods are available for charting alternatives: forked flow-lines; footnotes; or construction of an additional flow-chart.

Forked flow-lines are generally preferred; however in some can be difficult to incorporate, or result in an extremely crowded, complicated chart.



Footnotes may provide a solution; however important procedures are easily obscured by removal from the visual impact of the chart, to a footnote.

Similarly, creating a **separate flow-chart** can sometimes be the clearest solution, but the additional pages may result in extra effort for the flow-charter or create confusion for the reader.

Overall, your decision should be guided by what you believe will be simplest to draw and easiest to understand when drawn.

Planning of layout

Preparing drafts before actually flow-charting can greatly improve the final product.

Possibilities to bear in mind when drafting are:

rearranging column headings;

varying the initial order of documents in sets; and

changing the overall layout (for example, placing the second Start Point above the documents flowing from the first).

Wherever possible, the order of a set should be kept consistent once it is first shown.

Presentation

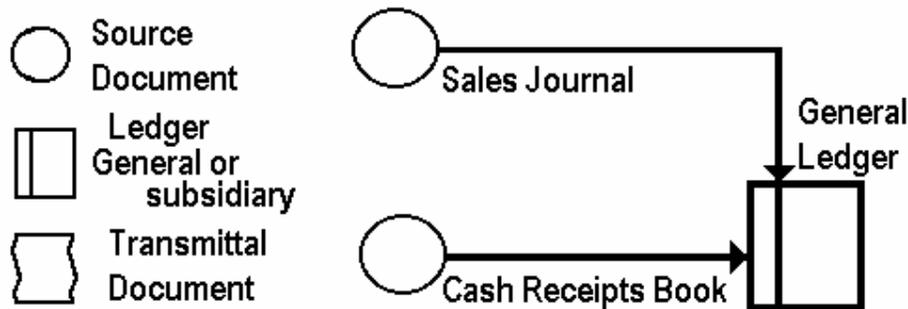
The finished flow-chart should maintain consistency with regards to the slope, order and spacing of sets; and the more symmetrical the layout can be made, the more pleasing the end result will appear.

Accounting system symbols

These symbols are little used in Customs / Revenue flow-charting when we are generally auditing transactions in the physical system (eg control of goods), rather than dollar amounts in the accounting system (eg total dollars invoiced for a year.) The symbols for source documents, transmittal documents and ledgers refer to the general accounting terms. These documents could also be shown by the symbols given earlier, if the emphasis is not being placed on the accounting system.

The accounting symbols are only likely to be used in more complex audits, for example, to support an analytical check which focuses on the accounting system, its workings and final dollar output.

The basic principles for showing the movement of documents and information flows are the same. These symbols, with a simple example, are illustrated below.



Computerised flow-charting Depicting computer systems

A number of additional symbols are involved, to depict the system itself, information input media (visual display units etc), the data storage media (hard disk or external files), and the movement of data within the system.

These are shown below and at 5/5/2.

Note: in contrast to the broken flow-lines used to show information movement among documents, the flow of data within a computerised system, and to a printer to generate a computer printed document, are unbroken lines.

Charts sometimes use broken flow-lines within computer systems for clarity. While this is not incorrect, it is not usually necessary in all audits to pursue the fine

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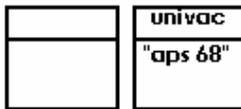
distinction between raw data and processed information; consequently, solid flow-lines are best used, for consistency.

Flow-lines between the elements of the computer system may run diagonally where required.

The end result of flow-charting a computer system for audit purposes will **not** resemble the chart that a computer systems engineer would produce. Our key interest is in the end results of the operation of the system, which affect the audit, rather than its detailed mechanics.

The extent to which you dissect and depict the workings of a computer system will depend on the nature of the audit. However, in most cases, it is sufficient to identify the computer, the system in use and the files involved.

Computer systems flow-chart symbols

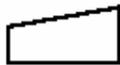


The **computer process** symbol shows the name of the computer used by the company, at the top and the particular system involved in a function at the bottom of the box. A note is usually included to indicate the function done (eg 'updates sales') adjacent or as a footnote.

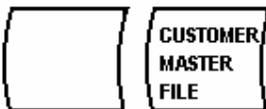
Since the emphasis is on what the computer **does**, rather than where the visual display unit etc is situated, it is common to find a computer system reproduced on another part of the chart, where a different process is carried out. This also allows a clear representation of which files are used for which process.



Visual Display Units include all terminals where the operator receives feedback from the system.



Computer Data Entry Unit symbol is used for a terminal that does nothing except accept input. These are not common; the type most often encountered are those at remote petroleum terminals, where the driver inputs load details to a terminal which gives them no feedback other than accepting the transaction.



Internal Computer Files symbols show information storage files internal to the on site computer, and

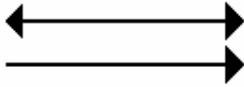
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External Computer Files show information storage other than the hard drive. These would include floppy disks, tapes and CD ROMS.



Backups which are indicated where relevant for internal control purposes.



Data flow can be one- or two-way, as indicated by data-flow arrows.



The **electronic data transmission** symbol should be used when a modem or dedicated landline transfers data from one physical site to another.

**Sampling
Standards and practices**

When using either a statistical or a non-statistical sampling approach, the auditor should design and select an audit sample, perform audit procedures thereon and evaluate sample results so as to provide sufficient appropriate audit evidence.

When designing an audit sample, the auditor should consider the specific audit objectives and the attributes of the population from which the auditor wishes to draw the sample.

Judgemental sampling

Customs / Revenue has adopted Judgemental Sampling for Customs / Revenue Audit Methodology. Therefore, auditors need some understanding of what judgemental sampling means in relation to the:

- choice of a sample size;
- choice of a sampling technique;
- determining of the population size; and
- interpretation of the results.

The most important feature of judgemental sampling is the interpretation of the results of the tests performed.

These results are not used to form any mathematically precise opinion as to:
the size of the problem if errors are encountered; or
the degree of precision with which results can be stated.

Compliance testing

Where a test is designed to check if a control is working (compliance tests), the result of the test is used by the auditor to decide whether the control is, or is not, reliable. This will influence the auditor's judgement when determining the sample sizes to be used when testing the validity of the company's records, ie when performing substantive testing.

Examples of compliance tests are:

- tariff classification checked by senior broker/consultant;
- correct tariff rates are applied and the correct amount of excise paid;
- costing/valuation of imported materials is to be used in the manufacture of other goods are checked back to supplier's invoice;
- checking that there is evidence that stock-takes have been performed;
- checking that there is evidence that meter calibrations have been performed; and
- checking that there is evidence that a quality control check has been performed.

Evidence in these cases would normally be the recording of:

- the name and signature of the person doing the activity (eg performing the check);
- the date the activity was performed; and
- the result of the activity.

Substantive testing

In the case of substantive testing, the result is used to assist the officer to form an opinion as to whether he or she considers that the audit objective/s is being achieved.

Examples of substantive tests are checking that:

tariff items are correct;

valuation is correct for imports;

concessions claimed are appropriate;

the goods or packaged product recorded in the stock register or stock control system as being on the premises can be located;

duty free and under bond deliveries are only made to appropriate premises or vessels;

the raw material stated as having being used has been correctly recorded as input to production runs; and

the ratio of production yield to raw material usage is reasonable.

Sample size

When using judgemental sampling, the recommended sample size to be used need not be strictly adhered to. It can be adjusted based on the auditor's professional judgement as to whether more or less testing is required to reach an acceptable conclusion. However this should be done only with the explicit approval of the audit team leader (refer also to paragraph 2/6/3).

Discovery sampling

The sample sizes for both compliance and substantive testing included in Sub-section 2/6 have been set using what is referred to as a 'discovery' sampling approach. This means that if any errors are detected then it must be assumed that there is a potentially significant problem.

This means that, for compliance testing, if an error is found then the officer cannot put any significant reliance on that control functioning correctly.

If an error is found in a substantive test, the officer must consider the possibility that there are a number of such errors in the total set of records being looked at.

If, however, no errors are detected then the sample sizes in the chart will allow the officer to have a very high (about 95%) level of confidence that the result is representative of the entire population being sampled. This level of confidence will normally be based on a combination of the officer's observations, the results of analytical checks performed, the results of tests of controls performed and the substantive tests performed.

As can be seen from the above discussion, judgemental sampling is not intended to be as precise in its analysis of results as is statistical sampling. This approach means that there is more flexibility in the sampling process used.

The main requirement in the selection of the sample is that it is adequate to enable the officer to make the required assessment or to form the required opinion concerning the total audit period.

Audit Training and Capacity Building

The remainder of this chapter will discuss the techniques available to officers to achieve this requirement in a way that does not waste time.

Choosing a sampling technique **Sampling techniques available**

The key factor to be borne in mind when considering the method of sampling to be used is that the sample should be representative of the total population being examined. This means that, to the maximum extent practicable, all items in the population should have an equal opportunity to be selected.

There are a number of sampling techniques available to achieve this:

random-number sampling;

systematic (interval/skip) sampling;

block sampling;

stratification sampling

dollar unit sampling

haphazard sampling; and

stop and go sampling;

or a combination of two or more sampling techniques.

(Refer to the flow-chart of sampling process at Paragraph 6/6/3)

Attribute sampling

All of these techniques are types of what is called 'attribute' sampling. They will only enable an assessment to be made regarding the occurrence of an error. They will not enable any assessment to be made about the significance of the error.

This is fine when they are used for compliance testing as the test is only being performed to establish whether the control has, or has not, been applied.

Where these techniques are used for substantive testing care must be taken not to attempt to place any significance on the value of the 'sampling unit' in error.

All errors must be given equal significance. For example the fact that a tariff concession order is used incorrectly on a low value line is worth only a few dollars, does NOT mean that the error can be ignored. It must be considered that it is indicative of an unacceptable error rate, which could apply equally to the large value items as the small value items.

Later in this section, techniques are briefly discussed which do allow assessments of the value of the errors to be made. Of these the use of stratification with the 'attribute' sampling techniques discussed in this section is the only one that may be practical unless the officer has access to a copy of the organisation's computer data and to a computer system to process this data.

Determining the appropriate sampling selection process

The steps in determining how a specific compliance testing or substantive testing sample is to be selected are found at the end of these notes. This process is based on the use of 'attribute' sampling techniques.

Random number sampling

Random number sampling is based on the use of a random number generator or random number tables to select the items to be tested. It is first necessary to establish the start and end numbers for the population to be sampled. This method assumes that:

the units in the population, ie the 'sampling unit', are sequentially numbered; and
the units are stored in sequential number order.

If these two assumptions are not met then this technique will require a large amount of effort to allocate or locate sequential numbers. It is unlikely that auditors will find instances of consecutively numbered documents that are filed consecutively in any case.

Systematic sampling

Systematic sampling is sometimes also referred to as interval or skip sampling. It involves selecting every 'nth' item in a population, where n is the sampling interval, starting from a randomly selected item. Systematic sampling is based on the officer:

determining the population size and sample size;
establishing a sampling interval by dividing the sampling size into the population size;
randomly selecting a start point in the first sampling interval; and
selecting the 'sampling units' located at the start point and at subsequent sampling intervals from the start point.

One of the key steps is determining the population size. This may not always be easy; for example if the officer is faced with a number of filing cabinets of documents. In such cases, the officer should not attempt to count all of the documents. Using measurement techniques, or at worst simply guessing, the officer should obtain an estimate of the size of the population.

In some cases, it may be appropriate to use a combination of the systematic and random-number sampling techniques.

Rather than estimating the number of lines in multi-line documents over the period and counting lines to select the population, the following technique could be used:

estimate/guess the population size for the population of documents;
select a sample of documents using the systematic sampling technique; and
randomly select a line from the document using the random-number technique.

Block sampling

Block sampling involves the selection of a number of grouped 'sampling units'; for example checking all transactions for selected dates.

However, even with judgemental sampling, care needs to be taken with the use of block sampling to ensure that sufficient blocks are selected to be able to reach a

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reasonable audit conclusion for the total period being audited. Selecting one or two small blocks over a large period will not achieve this, eg one or two weeks over a twelve-month period.

Another possible method of sampling would be to:

determine the number of days in the period;
estimate/guess the average number of lines per day;
randomly, using random-number or systematic sampling, select a number of days judged to give the desired sample of lines; and
check all 'sampling unit' lines on all forms for those days.
Adjustments could be made to the number of days during the test process to avoid major over or under-sampling.

Haphazard sampling

Haphazard sampling is defined as 'sampling units selected without any conscious bias'. It should be selected in a manner that can be expected to be representative of the population. However, it does not require any form of systematic selection. Estimate/guess the boundary of the first sampling interval, ie the forms to be included, pick a form in this interval and pick a line in the selected form; and Repeat the above step until the end of the forms was reached.

Adjustments may have to be made to the sampling interval boundaries while sampling to avoid over- or under-sampling.

However, care must be taken to avoid distorting the sample by selecting, for example, only unusual or physically small items or omitting items such as the first or last items. This technique must not be used as a way of avoiding 'difficult' items. It is possible to use any of the above techniques or any combination of them. Whichever technique is used it should achieve the goal of being representative of the total population. (Note: It is essential that the method used to select the sample be documented.) It should also be noted that with judgemental sampling there is also scope for:

including in the sample items of special interest, which are noticed while selecting the sample. Their specific inclusion is to be documented so that the person evaluating the results is able to reach a judgement as to their relevance to the assessment of the total population; and

a management decision to reduce the level of testing if it is considered that, based on past experience, observation and analytical procedures, the company is reliable and trustworthy.

Small populations Correction formula

The sample size adjustment formula (Finite Correction Factor) can be applied if the determined population size is less than 2,000. For population sizes above this its effect is marginal.

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The formula, where **Sample size = A**, and **Population size = B**, is:

$$\text{Adjusted sample size} = A / (1 + A / B)$$

Where it is known that the population is relatively small and that almost all of the population will be included in the sample even after applying the adjustment formula, a decision to perform sample checking or 100% checking needs to be made. This decision should be based on the most effective use of resources. It will depend on the overhead cost associated with the sample selection technique being used. This is a matter to be resolved between the auditor and the audit team leader. However, the reason for a decision to proceed with 100% checking is to be documented in the working papers.

Variables sampling and stratification

Introduction

It should be noted that all of the sampling techniques described above are what are referred to as ‘attribute sampling’ techniques. They are aimed at detecting occurrences of error. They are not aimed at giving any indication of the importance of the error.

What this means is that no errors detected can be ignored even if the value of the goods or product associated with the error is small. This is because it is as indicative of a significant possible problem with the licensee's records as would be an error with a large dollar or quantity value.

Variables sampling

There are ways of sampling that would provide an indication of the value associated with the errors such as the classical variables statistical sampling technique. However, the application of these techniques would not be practical unless the company has computerised records and these can be input into a computer based sample selection system.

Stratification

There is also a way of breaking up the population, referred to as ‘stratification’, which will enable the sampling techniques described to be applied in such a way as to provide an indication as to the possible significance of the error.

Stratification of a population of records is the process of breaking up the population into sub-groups. This can be done to achieve sub-groups for which all of the records have about the same dollar or quantity value. It is suggested that the following broad stratification strategy be applied:

- identify those items, for example above a set dollar value, which it is considered should all be checked;
- identify the grouping of items which are significant and which should form the majority of the sample, say about 80% to 90%; and

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identify the remainder of the population which is of less significance and which would need to involve a large number of cases of error or fraud to result in significant revenue due not being collected. Only a small percentage of the sample would be expected to come from this sub-group.

If it is possible to apply this break up to the substantive testing being performed then the testing will be biased towards the more significant items.

This approach should only be considered when the stratification could be easily achieved. This will not usually be the case unless the licensee's records are computerised.

Interpreting sample results (materiality)

Definition

Simply put, materiality of errors detected in a test is an assessment of how important that error is. It is best to consider this issue separately for compliance and substantive testing.

Compliance testing

The purpose of a compliance test is to establish whether a control can or cannot be relied on to ensure that the related audit sub-objective is being achieved.

For example, if a check is being performed to ensure that the required stock-takes had been performed and that any discrepancies were noted and reported, there could be several errors detected:

one or more stock-takes were not undertaken;

the stock-takes were undertaken but there is no record of the actual stock counts recorded for one or more of the lines of goods that were supposed to have been checked;

the stock-takes were undertaken accurately and completely but there is no evidence that any action was taken in regard to one or more discrepancies found;

the stock-takes were undertaken accurately and completely and discrepancies have been actioned but one or more of the stock-take sheets have not been correctly signed and dated; or

the stock-takes were undertaken accurately and completely, discrepancies actioned and the sheets correctly signed and dated but one or more of the stock-takes were undertaken by the storeman.

The materiality of the errors would relate to the extent to which the errors reduce the auditor's ability to rely on the record of stock-takes to provide an assurance that the stock register is a complete and accurate record of goods in storage.

There is no sampling involved in this test. In this case, the auditor must simply decide whether the nature and extent of the errors found reduces his or her confidence in the accuracy and completeness of the stock-takes to detect discrepancies and ensure these are reported. In some cases, this is a simple assessment. If for example, a single stock-take is involved, and this has not been performed or has not been performed correctly or completely, then there can be no confidence in this process. In other cases it is a subjective judgement; for example if signatures are missing.

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Where the test involves the selection of a sample and errors are detected then an assessment needs to be made as to whether to:

discount the error;

increase the sample size; or

place less reliance on the control.

For example, suppose a sample of 100 duplicate invoices was selected to check that an independent clerk has initialled the duplicate invoice as proof that they have verified the quantity, price and excise item on invoices.

If it is found that one invoice has not been signed, it may be decided that even though this results in a slight increase in the risk that the control may not be being applied consistently to ensure that goods are entered correctly, a reasonably high confidence level is still appropriate. However if 10 errors are found it may be decided that only a medium level of confidence is appropriate. If 20 to 30 errors are found it would probably be decided that the control was not reliable ie a low level of reliability was appropriate.

If the initial sample was 30 invoices (as per the Compliance Testing sample chart in 2/5/3) in the sample above and one or two errors were detected the officer will need to make a decision to either:

extend the sample size to 65 or 100 (as per the chart) and see how many more errors are detected before making a decision on the reliability of the control; or

decide that the control is not to be relied on for the purposes of this audit; ie give it a low rating.

The decision should be made in consultation with the audit team leader. If the control is important then it would be appropriate to increase the extent of testing to 100 invoices so that an assessment can be made of the control and adverse findings discussed with the company.

Substantive testing

An error in a substantive test means that a record has been found either incorrect or incomplete. This will usually have a potential revenue implication or other non-compliance outcome.

If even one such error is found in a sample of 50 items being checked then the officer should increase the sample size to 100 unless the errors are very clearly isolated and explained incidents or an error is of minor significance compared to the value of the record being checked.

If errors are found in a sample of 100 or 150 then the officer needs to make a decision as to whether the increased risk of error in the total population could be materially significant. As a guide the following table should be used:

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Sample Size	Errors Found	Possible Error Rate
100	1 or 2	6%
	3 to 5	10%
	6 to 10	16%
150	1 or 2	3%
	3 to 5	7%
	6 to 10	11%

For example if in a sample of 100, two errors were found it would need to be decided if an overall 6% error rate in the total population being tested was materially significant. This may be 6% of entry lines being incorrect or 6% of production not being accounted for, etc. If it is considered that this error rate could be significant then the sample size should be increased to 200. This is done to get a true feel for the extent of potential error.

When sampling at the 200-item level and errors are found the officer must refer to the CTM for a decision as to further action. This could possibly involve 100% checking. As a guide, the following approaches may be useful if any estimate of the possible materiality (ie significance) of the errors in the total population is desired:

Approach A:

Using the following table assess the significance of the overall materiality:

Errors Found	Possible Error Rate (Records in Error)
1 or 2	3%
3 to 5	6%
6 to 10	8%

(This is only a very rough 'guesstimate' based on the high confidence level being used).

Approach B:

This approach is feasible only if it is possible to place a quantitative value (dollars or quantity) on the errors detected (both options) and on the items being checked and the total value of the population (Option B.2). In this case, one of these options can be considered.

B.1 - If the items in the population all have a similar value:

Add up the total value of the error in the sample;

Divide this by the sample size (ie number of items in the sample); and

Multiply this figure by the total population size (number of items in the population).

B.2 - If the items in the population have a significant range of values:

- (a) = total value of errors in the sample (eg \$1,000)
- (b) = total value of sample (eg \$6,000)
- (c) = total value of population (eg \$60,000)
- (d) = proportion of sample to population
= $b/c \times 100$ (eg $6000/60000 \times 100 = 10\%$)
- (e) = extrapolation of value of error to whole population
= a/d (eg $\$1000/10\% = 1000/10 \times 100 = \$10,000$)

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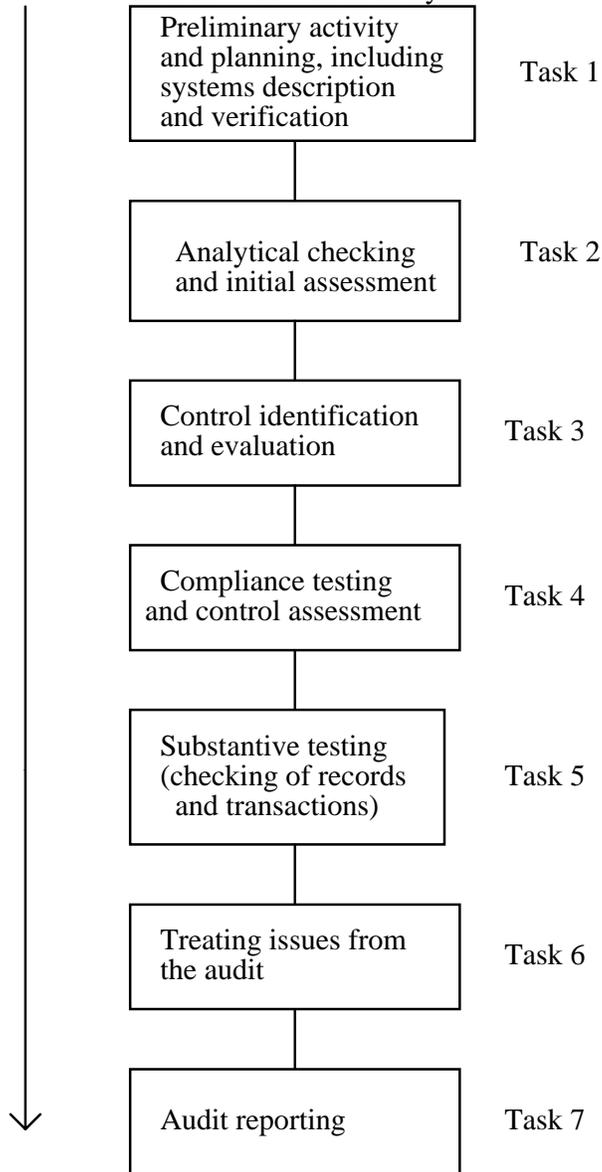
When considering the materiality of an error in a substantive test consideration needs to be given to the nature of the error, eg is it an isolated and explained event or is the error of minor significance when compared to the value of the record being checked. However, if attribute sampling is being used consideration should not be given to the value of the record in error, ie it is not possible to say that the error is insignificant because it only related to a small value item.

It should also be borne in mind that Customs / Revenue has set a high standard for what it wants to achieve in regard to obtaining an assurance that revenue due is being collected when it falls due. The sample sizes given on the charts in this section are aimed at achieving this standard. This standard needs to be maintained. Thus if even a small number of errors are found but it is considered that this could be indicative of a significant revenue gap, this should be followed up.

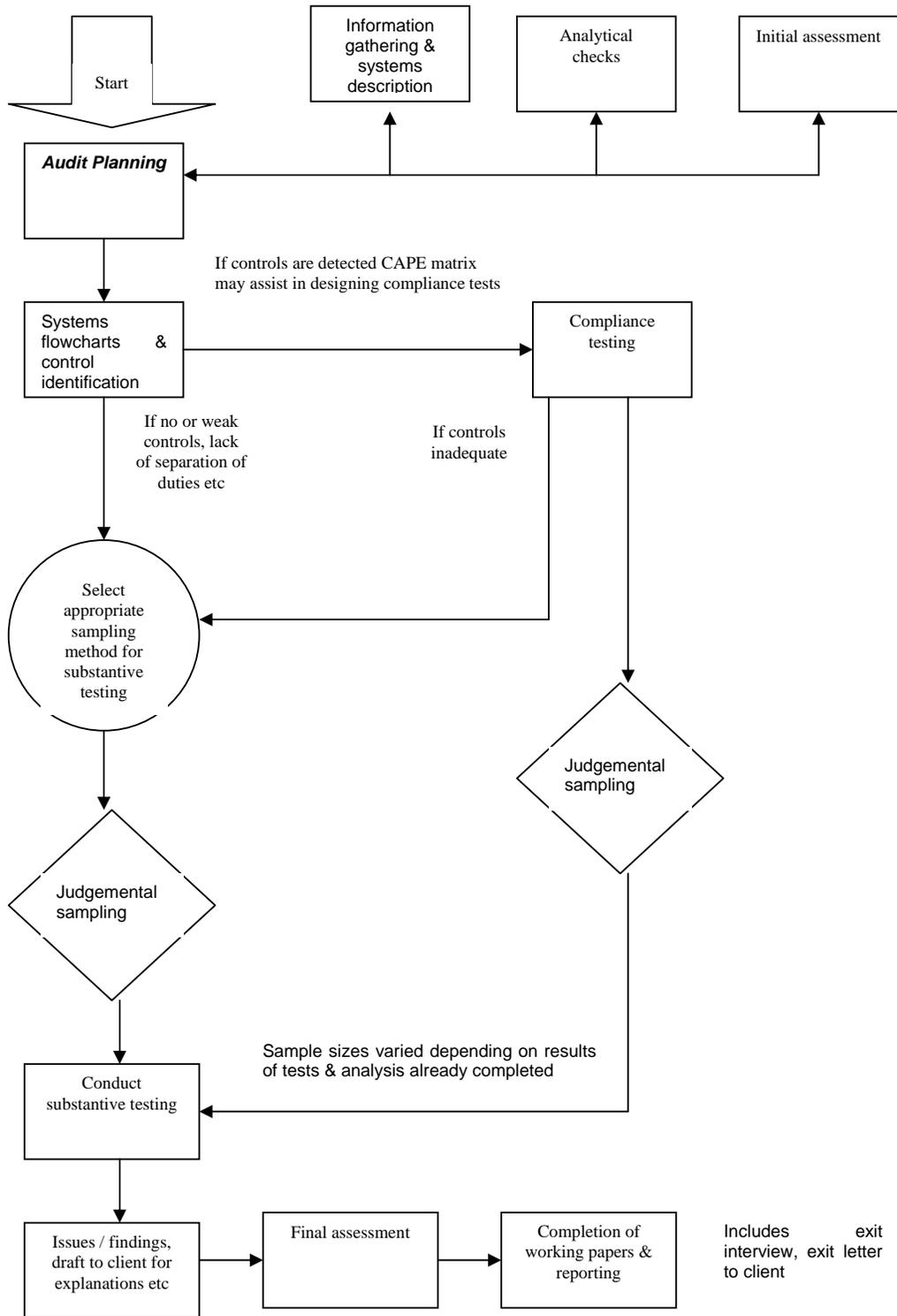
A sampling flow-chart, which shows the decision points in the sampling process, is shown on the next page.

Audit Methodology

The following diagram and flow-chart are examples representing the flow of Audit Methodology (different circumstances may warrant changes to the order or detail outlined below). These should be modified to suit your circumstances.



Audit Process Overview



Task 1 - Initial activity and planning

The extent of the work performed at the preliminary activity stage will vary from audit to audit depending on the information included in the activity kit and the audit team's previous experience with the client's operations and its complexities. Regardless of whether the preliminary activity is performed elsewhere or whether it is performed by the Compliance Team, this stage forms the basis of the audit process and is a key element to the production of an efficient audit approach.

Objectives

The objectives of the preliminary activity stage are to:

- understand and record management expectations and any specific concerns;
- clearly specify the objectives, scope, focus and coverage of the audit;
- establish a cooperative relationship with the company management in regard to the conduct and expected outcomes of the audit;
- obtain an overview of the company to be audited by identifying all relevant significant operational and information systems;
- write to the company and inform them that they have been selected for audit and that Customs / Revenue will make contact in the near future to arrange a time for a formal Entrance Interview;
- decide on the sites to be visited; and
- produce an audit plan that includes a time-line for the audit, noting resource allocations.

The major outputs from the preliminary activity stage are:

- a summary of management expectations and concerns;
- a preliminary understanding of the company under review;
- an overview of the company's systems (using notes and/or flow-charts); and
- an audit plan including objectives and a time-line for the audit.

Steps to be conducted to complete task 1

The steps to be carried out in the preliminary activity stage are:

- Obtain and evaluate background information available in office and establish audit objectives, scope, focus and coverage.
- Conduct the Entrance Interview.
- Perform information gathering and familiarisation activity in the company's Head Office - include systems description and verification.
- Decide on the approach to be taken.
- Develop the detailed audit plan - include audit time-line and resource allocation.

Step 1 - In-office activity

As the first step Task 1, the auditor/researcher will seek to obtain and evaluate background information available within Customs / Revenue on the company to be audited. Background information can be obtained from a number of sources such as:

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any previous systems based audit (SBA) or other audit reports and working papers;
any permanent company files;
discussions with other auditors who performed the previous audits;
discussions with other relevant areas of Customs / Revenue in relation to any anomalies, specific areas of concern or special coverage to be examined/covered by the audit team;
interrogation of Customs / Revenue databases; and
interrogation of external databases.

The statement of audit objectives, scope and focus to be addressed during the audit is produced at this stage. For example:

to conduct a systems based audit on all company systems as they relate to Customs / Revenue;
to conduct a focussed audit on usage of a particular concession; or
to conduct a follow-up audit on issues which were raised in the report of a previous audit.

The objectives of the audit will result from the consideration of any management concerns and the requirements of any important issues raised during Step 1. The audit objectives will generally be determined and conveyed to the Compliance Team although additional in-office activity may still be performed by the Compliance Team.

Step 2 - The Entrance Interview

After obtaining and evaluating all available in-office background information, the auditors will need to familiarise themselves with the operational and financial environment of the client and understand the company operations.

The first meeting with the client 's senior management is the Entrance Interview. The client 's agent, consultant or lawyer may also be present. This meeting provides the opportunity for the auditors to:

explain the purpose of the audit to the company management;
foster the goals of Customs / Revenue by jointly discussing the philosophy of Commercial Compliance;
discuss and document any concerns regarding internal controls.

This can be achieved by asking the following question *'Are you aware of any potential issues or problems relating to Customs / Revenue payment or legislative compliance which have been identified by the company or its auditors?'*; and deal with administrative matters such as the general audit timetable, identification of the company's contact officer for the audit and the organisation of site visits.

This also includes such logistic issues as contact with agents/consultants, accommodation for the audit team, identifying the location of records and gaining access to computer systems and data.

Where the audit team is to use contracted expertise on the audit; this should be brought to the attention of the company management at the Entrance Interview.

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Step 3 - Information gathering and systems description and verification

This step consists of a number of components. It is possible in most situations to complete each component concurrently as the audit team moves through the

company's systems.

Information gathering

The audit team will need to understand and document, by narrative and/or flow-charts, the company's systems that relate to Customs / Revenue. This includes how products, documents and data flow through the company.

During this stage the auditors should obtain an understanding of the company's organisational structure and identify those areas that have a direct or indirect relevance to the audit objectives. For example, groups responsible for performing relevant monitoring activities.

This level of understanding will be gained by interviewing the relevant company management who should understand the overall scope and purpose of the systems and by reviewing any existing systems documentation.

This should be followed by the interview of appropriate staff at the operational area. For example, line management, technical (eg Information Technology) or business managers (eg operations) as necessary. The auditor should be aware that controls management think are in place may not actually be put into practice by staff.

Review of applicable documentation such as procedure manuals and instructions, computer system descriptions and control manuals should be included at this stage.

When performing the preliminary activity the auditors should try, through discussion with management, to understand how management assure themselves that significant problems are not occurring. By asking the '*What can go wrong?*' questions and '*How do you know that this is not happening?*' the auditors can identify the controls relied upon by management.

Other possible sources of information, which may be available with the agreement of company senior management, are:

relevant internal audit reports and discussions with the company's internal audit staff;
relevant risk assessments performed during the annual external financial audit cycle phase; and
external audit management letters and reports and, possibly, discussions with the external auditors.

Documenting the system

The auditor's understanding of the system needs to be both clear and accurate to enable identification and a detailed analysis of the existing internal controls.

It is important to document adequately your understanding of the system to support subsequent control analysis and to enable effective quality control of work undertaken.

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Where available, for example, a previous systems based audit's working papers, existing documentation should be reviewed, and updated to reflect any changes.

Where the auditor is using the results of a previous SBA, the auditor should interview relevant company staff to obtain step by step verbal confirmation of any changes that may have taken place to the system as documented. These amendments may be changes to the computer systems, staff responsibilities or manual controls and procedures.

An appropriate combination of narrative and flow-charts helps to identify all relevant processes and data flows. In some instances, a simple narrative will suffice.

The advantage of assessing business product and data flows is that these are unlikely to change even if other changes, such as computer system updates, occur. Only if the business processes change will the documentation become irrelevant.

It is important to keep in mind that the purpose of documenting the system is to document internal company controls that are in place within the system. Processes and dataflow being documented should be directly relevant to the objectives of the audit. Describe only those systems that are relevant to Customs / Revenue business.

Identify the system processes

The auditor should obtain an understanding (through observation, interviews and review of available documentation) of the critical processes which make up the system. The level of detail required would vary with each audit but the auditor must have sufficient understanding of the systems to be able to identify those controls relevant to Customs / Revenue.

Conduct systems verification

Systems verification can be achieved by conducting walk-through tests or examining system documents filed in the permanent files identified in flow-charts/narrative.

Walk-through tests are used to confirm the completeness and accuracy of the auditors' understanding of how a significant transaction is processed, or how product storage and movement is controlled, and will complement the discussions with management noted above. The exact technique employed will depend on the nature of the system, type of evidence available and the audit objectives.

In executing a walk-through, the auditor should trace a transaction through the processes as documented in the flow-charts and/or narratives. A sample size of one may be sufficient to clarify understanding on any one particular process.

Having walked through each significant process, the auditor will be in a position to assess whether the systems description is correct.

Where audit activity is being undertaken at several sites, this walk-through check must be undertaken at each site and local variations/ extensions noted. This is an essential component in the system documentation stage as a location may have

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adopted 'local procedures' which either enhance or detract from the documented procedures.

Step 4 - Deciding on the approach to be taken

At some time during the preliminary activity stage of the audit, a decision needs to be taken on the approach to be adopted during the audit. The options include continuing with a full systems based approach or adopting a transaction based (substantive testing) approach.

If a full systems based audit approach is found inappropriate, then this fact should be documented in the working papers with the reasons to support this decision. At this point, the matter should be referred to the audit manager for his/her endorsement.

The audit will now be primarily a testing of relevant transactions or records which allow the audit scope and objectives to be met. The audit team should now complete an audit plan as discussed at Step 5 below 'Development of the Audit Plan'. The transaction based approach to company audit is as per Section 6 'Substantive Testing (checking of records and transactions)' and tasks 2, 3 and 4 should be by-passed.

Control and Potential Error (CAPE) Matrix

Policy for the conduct of systems based audit is to follow the CAPE approach. A suitable format for CAPE is found on working paper AUD05.

CAPE approach involves the auditor initially documenting the potential errors that could occur. The auditor then identifies and documents the actual controls and assesses whether these controls are adequate to reduce the risk of each of the potential errors to an acceptable level.

The concern with this approach is that if the auditor fails to initially include significant potential errors, then the audit conclusions may be incomplete. It also assumes a level of audit experience, which will ensure that relevant controls are identified, documented and correctly assessed.

A standard model for computer systems has been included in Section 5. It should be noted that this is a comprehensive generic model. It would need to be tailored both in relation to the nature of the system being audited and the specific potential errors that are of concern to Customs / Revenue.

Identify potential errors

During this stage, the auditor identifies the potential errors associated with the controls for the system under review. The steps involved in the identification of potential errors are as follows:

for each control, identify any error that affects Customs / Revenue. These 'what can go wrong's' are potential errors. It is also useful to consider, from a management perspective, 'what must we get right' when carrying out this analysis;

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in completing this exercise it is helpful to consider each significant transaction separately. In tracing transactions through each process, consider the type of processing carried out (ie initiation, amendment or transfer of data) and what significant information is required in order to provide the output of that process. For example, posting duty liability in relation to sales transactions may require the sales transaction volume data and duty rate data from the product master file. If the master file data is wrong, eg due to the rate of duty applicable being wrong, the risk to Customs / Revenue is that duty will be calculated incorrectly; and record the potential errors on the appropriate CAPE work-sheet (AUD05).

If it is only possible to identify vague or unspecific potential errors, the auditor should review the initial documentation to ensure that there is sufficient detail. The system documentation should be revisited to consider whether one or more processes or transaction types should be divided up into smaller sub-systems.

Step 5 - Development of the audit plan

It is important during the planning phase of the audit to develop a time-line for the audit showing major resource allocations. This would usually be put together by the audit team leader once the details from the preliminary activity are known.

The time-line should show the major tasks of the audit and give an indication of their likely commencement and completion dates. At this stage it is not possible to give an exact time frame for the audit as no control assessment has taken place and consequently the size of both compliance and substantive testing samples is not known. Auditors should, however, have an overall opinion as to the strength of company controls.

In general, the detailed audit plan should include as a minimum the following:

the audit objectives, focus and scope;

the period under audit;

the sites to be covered; and

matters of potential significance/issues to be examined.

It will also include a reference to compliance and substantive testing, however, specific tests cannot be designed at this stage as the controls have not been identified or assessed.

To ensure the draft audit plan is appropriate before discussions with company management, the details of the plan will be reviewed and approved by the audit manager.

Task 2 - Analytical checking and initial assessment

Analytical checking

Analytical checks can be described simply as the comparison of relationships among financial and non-financial data. For example, ratio of duty paid to sales in an excise revenue client should this information be available. The results of the relationship calculations performed can then be compared with the historical records of similar calculations done over time for that industry type and with the results of similar checks in like organisations. Basically, the auditor is checking the overall performance of the organisations against expected performance.

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To illustrate the concept of analytical checks the following examples are provided:

trends in the amount of duty paid;
trends in returns of factory costs;
trends in quantity/values exported; and
the ratio of packaging input material to packaged product.

Initial assessment

Based on the information gathered, in office and at the company, and the results of analytical checks, the auditor now forms a preliminary opinion as to the level of confidence concerning the company's compliance.

This assessment is the auditor's general opinion of company reliability. It may be influenced by the auditor's reaction to: competence of staff; discussions with senior management; discussions with staff and the consistency of the information provided.

This opinion of general company reliability is expressed in terms of:

Low	Little, if any confidence
Medium	Reasonable level of confidence but with some reservations
High	Good level of confidence.

This assessment and the reasoning that lead to it are to be documented.

This assessment opinion will be used in conjunction with a control assessment to establish a sample size for substantive testing.

For an auditor to be able to state that he or she has a 'high' level of confidence there will need to be:

a history of audits performed with no adverse findings;
no significant system, physical environment or personnel changes since the last audit;
confidence that there are reliable, experienced company staff;
a set of analytical checks in place which provide a trend analysis for the organisation eg comparing excise paid to other factors over time; and
a set of analytical checks in place which provide a point in time analysis eg comparing the duty paid with industry norms and current economic and business performance indicators.

Without any of the above an assessment of medium or low should be given.

Kinds of information considered during the initial assessment.

After gathering information and performing analytical checks, the officer is now in a position to form a preliminary opinion as to the level of confidence he or she has that all Customs / Revenue requirements are met by the organisation being audited. The opinion to be expressed has already been discussed.

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When forming a preliminary opinion the auditor could take into account inherent risks such as:

- results of analytical checks;
- company's audit history (Customs / Revenue audits, internal audits, external audits);
- competitiveness within the industry;
- revenue liability involved;
- knowledge of key personnel with respect to Customs / Revenue requirements;
- knowledge of key personnel with respect to goods imported;
- results of interrogation of Customs / Revenue systems;
- changes in the activities or performance of the client ;
- whether the company or broker/agent has conducted an internal review.

Task 3 - Control identification and evaluation

Internal controls

The CAPE matrix approach takes into consideration the strength of the internal company controls. Consequently, these controls need to be identified and evaluated. If sufficient internal company controls cannot be identified it is inappropriate to attempt to use a systems based audit (SBA) approach. In this instance, a transaction-based approach (substantive testing) would be used which may involve the checking of a larger number of transactions.

At this stage, the auditor is making a comparison between 'what should be' with 'what is'.

The first part of this task is to identify and evaluate the actual controls in the system from documentation compiled in the previous tasks. The actual controls are then recorded on the CAPE matrix (AUD05) work-sheets as appropriate and the control evaluation is then performed on the relevant work-sheet (AUD05a). Key controls identified at this stage then become the focus of audit testing.

Identify actual controls/preliminary evaluation

Using the system description compiled during preliminary activity, the auditor should look for actual controls in the system, which should then be documented on CAPE matrices (AUD05).

For each control these work-sheets should:

- detail the type and frequency of the control;
- identify whether it is a preventive, detective or corrective control;
- note who performs the control;
- identify whether the control is manual or computerised, and
- undertake a preliminary evaluation of the effectiveness of the control.

Preliminary control assessment/evaluation

With each control identified, the auditor needs to consider its impact (if any) on each of the potential errors. This is known as the preliminary control assessment.

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The evaluation of the effectiveness of controls is a critical stage in the audit. An assessment of the level of confidence in the effectiveness of the control is made ie. HIGH, MEDIUM or LOW confidence. This level of confidence will be based on: the information gathered up to this stage of the audit; and examination of the CAPE matrix to gain an opinion of how the controls impact on potential errors.

This evaluation is called a Preliminary Control Assessment because it has not yet been tested. It is only after testing the controls that the auditor's assessment can be confirmed and a final control assessment can be made. Please note that this is not the initial assessment referred to previously.

The auditor tests controls in order to establish whether the auditor's assessment of controls is correct. This is called Compliance Testing. The Preliminary Assessment of High, Medium or Low will be used to establish a sample size for compliance testing. After testing, the controls need to be evaluated again to determine the

substantive test approach to be taken. Control evaluation using matrices

Generally, the auditor should use one CAPE matrix work-sheet for each sub-system. Form AUD05 should generally be used for control evaluation.

Once the auditor has part-completed the CAPE matrices and identified the potential errors for each sub-system, they need to consider and evaluate the controls that have been put in place.

The objective of this task is to consider the potential errors and determine whether effective and efficient controls have been established to prevent or detect the potential errors (or whether controls that are needed are missing).

In some complex systems, many of the controls identified will be dependent on controls operating within and over the computer environment, such as data file access controls or program change controls. The auditor will either evaluate these controls, or rely on previous work done on this area. In order to evaluate these controls within computer systems it may be necessary to use Information Technology specialists. When identifying controls, the auditor should take account of both preventive and detective controls. Management will often require a combination of controls to adequately satisfy themselves that the identified risk is appropriately minimised. It is vital that controls are functioning effectively to prevent or detect errors. Whilst detective controls such as Customs / Revenue audit testing are more costly, controls such as regular analytical comparisons including ratios could be more effective than many preventive controls applied to each account or transaction.

Having identified the controls, these are documented on the CAPE matrices against the related potential errors, identifying the type of control (ie preventive or detective).

Identify reliance on computer controls

Many of the controls in systems on which management rely are likely to be programmed (computerised) controls. These are controls carried out by a computer

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program or dependent upon computer produced information. Examples of such controls are:

computer processes which perform significant calculations (eg Customs / Revenue liabilities for transactions);

computer controls (eg edit checks and reasonableness checks on input data such as raw material or product prices);

computer produced exception reports which are subsequently followed up manually;

computer produced management information which forms the basis of management detective controls; and

controls to prevent or detect access to standing data files (eg price data) by unauthorised staff.

The auditors need to identify reliance on programmed controls to determine the nature and extent of audit work to be carried out in the computer environment so that they are satisfied that the programmed controls are operating as designed.

Where the company relies on computer controls to address risks (identified on the CAPE matrices as a programmed control), the auditors need to obtain further information about the adequacy of the control and the control environment so as to avoid placing unwarranted reliance on computer processes or computer produced data.

We need to know how management satisfy themselves that the programmed controls are operating as intended, for example:

manual controls to confirm the adequacy of computer processing (eg reasonableness checks or clerical checks of a sample of calculations made by the computer).

However, this may be inefficient, given the nature of the control; and/ or

the underlying general controls over the computer environment (eg program/data change controls such as the testing of a program, the control over changes to that program and control over access to the master file containing standing data used within the program.

The auditor will need to liaise with the company's information systems auditors and computing staff in order to derive the most efficient audit approach for each audit.

Completion of cape matrix work-sheet

The CAPE matrices are used to record the nature of controls in place and address each specific potential error. Consequently all types of relevant controls should be documented (preventive and detective, computer and manual, general Information Technology controls) where they play a part in addressing a particular potential error.

The advantage of documenting all types of controls is that the CAPE matrices allow the auditor to analyse an efficient combination of controls. Through the documentation process, the auditor can identify weak control structures that can influence the quantity of testing subsequently conducted. This information can also be used as the basis of recommendations to the company accordingly.

It is important to ensure that descriptions of relevant Information Technology general controls (such as program change and data file access controls) are properly

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documented on the relevant CAPE matrix. For example 'Updates to the stock availability program are applied only by authorised staff', and 'Access to sales contract quantities on the master file is restricted to the sales accounting staff', may together ensure that final stock availability for any particular stock line is properly calculated. This detail ensures that the result is complete and gives the auditor additional insight into the existing controls.

The auditor must determine whether the identified controls, taken together, are adequate to address each potential error. A preliminary evaluation is recorded in the bottom rows of the CAPE matrix.

The evaluation is dependent on 'auditor judgement' taking account of:
the significance of the identified potential errors;
the quality of the identified controls; and
'Standards' level of tolerance.

CAPE matrix instructions

Identify potential errors (things that could go wrong with Customs / Revenue requirements). Describe them in the appropriate box below.

Identify controls in client systems (things that prevent or detect the potential errors). Describe them in the matrix.

Examine the manner in which the controls prevent (P) or detect (D) the potential errors. Place a P or a D in the box where the control affects the error.

Assess the impact of the controls on each potential error. Note your assessment in the 'Preliminary Adequacy of Controls' box.

If necessary, design Compliance tests and test the controls. Note the test number in the box on the far right hand side.

Based on the results of the testing, assess the adequacy of the controls as they affect each potential error.

Note your assessment in the box 'Control Assessment after Testing'.

Note the risk remaining in the appropriate box taking into consideration the post testing assessment of controls.

Determine whether substantive testing will be carried out. Note the substantive test numbers in the 'Substantive Testing Reference' box.

Evaluation results

On completion of the evaluation of controls, the auditor should identify the key controls that are significant in reducing the major risks. These controls would be noted on the appropriate work-sheets. These are the controls that would be subject to testing if they appear to be operating effectively at this stage.

The preliminary control evaluation has been made and recorded on the CAPE matrix work-sheet. This evaluation may need to be revised at the end of the compliance testing phase of the audit if it turns out that key controls which the auditor is relying on prove to be ineffective (ie compliance testing fails).

Each individual CAPE matrix should be evaluated by considering each column on the work-sheet to ascertain if there are sufficient actual controls to reduce the risk to an acceptable level.

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Any issues that arise from the evaluation should be recorded in the audit report. The control evaluation would be expressed as a level of confidence in the company's controls that is: High, Medium or Low. This will be used when deciding on a sample size for compliance testing.

Task 4 - Compliance testing and control assessment

The steps to be carried out in testing the system's controls are as follows.

Designing compliance tests

At this stage, the auditor designs the compliance tests to test the effectiveness of the controls. The major source of information for the design of each particular testing procedure is the description of each control previously recorded including:

the type and frequency of the control;
who performs the control;
identification of whether the control is manual or computerised; and
preliminary evaluation of the effectiveness of the control.

The design of a compliance test involves testing whether the control that is in place is working. For example:

if the control recognised in an excise compliance audit is that the accountant checks invoice values to ensure that the costing of imported excisable goods reflects the true invoiced price, the test would be to check an appropriate quantity of invoices for evidence (initial on document) that the control had been performed; and
if the control is a detective control such as a stock-take, the compliance test would be an examination of stock-take records to ensure that stock-takes have been carried out and discrepancies followed up.

Sample size for compliance testing

The extent of testing may be different for each of the compliance tests generated. It will depend on the level of confidence that the auditor has been able to obtain from: control evaluation carried out in Task 3 (High, Medium or Low); and information assessed in Task 2 - observation of the company's operations, discussions with staff performing the activities (High, Medium, or Low);
As a guide, based on this level of confidence, the auditor will decide which of the following levels of testing is appropriate for each procedure being tested:

High confidence	Light testing (30 items)	The auditor is confident that the control procedure is working and is only looking to confirm this.
Medium confidence	Medium testing (65 items)	The auditor is reasonably confident that the control procedure is working but is not sure.

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Low confidence	High testing (100 items)	The auditor is not confident that the control procedure is working and is looking to get some feel for the extent of non-compliance. In this case, the auditor may choose not to proceed with testing of the control at all and assess the control as being unreliable.
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The above suggested sample sizes apply to manual processing and manual controls. In a computerised processing and computerised control environment, one, two or three samples for every type of transaction may be sufficient, provided that the Electronic Data Processing controls are adequate.

If the light testing finds an error, the auditor may choose to extend the testing to the medium or high level. Alternatively, the auditor could decide not to place any reliance on the control. The auditor is expected to discuss the errors found and the proposed action with the audit manager. The final decision regarding the appropriate action lies with the manager.

Note: If the population size is less than 2,000 then a *Finite Correction Factor* may be applied to reduce the sample size.

A typical audit test plan work sheet would include the following:

- objective of the procedure;
- description of the testing procedures;
- type of test to be completed;
- level and extent of testing;
- basis for sample selection and sample sizes;
- the total sampling population and stratification definitions; and
- guidance as to the expected results of the work undertaken.

Guidelines regarding the selection of sampling techniques to be used are provided separately.

Execute tests of controls (compliance testing)

This stage confirms whether key controls are actually operational by executing test procedures as documented in the test plans prepared previously. It is not intended to go into detail on the performance of test procedures, since these will be specific to the scope of the audit in question.

Individual tests on the audit program should be indexed adequately as tests are completed. These should also be documented on the appropriate Testing work-sheets (AUD10).

Evaluation of compliance test results (control assessment)

Having completed the testing of each control, the auditor must make an assessment regarding the reliability of the control. Generally, if errors are found, and they cannot be shown to be isolated incidents due to some peculiar circumstance, then a high level of reliance should not be placed on the control.

The sampling notes provide a more detailed discussion of error materiality.

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When assessing the cause of errors identified, it is important to consider the possibility of fraudulent intent, for example to evade duty liability as well as accidental error.

Based on the results of the testing of controls performed, the auditor may need to reassess his/her opinion as to whether the company's system of internal controls is going to ensure that the relevant controls are effective.

The level of confidence in the company's system of internal controls is expressed as:

Low	Little, if any confidence
Medium	Reasonable level of confidence but with some reservations
High	Good level of confidence

When forming this opinion, the auditor will have to keep in mind the possibility of the company intentionally setting out to evade the payment of duty/tax due or compliance with licence or legislative requirements. This would mean that controls may appear to be operating but are being deliberately manipulated to hide activity that is not in accordance with licence or legislative requirements.

The extent to which this is possible or probable in the company being audited will be a matter of judgement based on:

the size of the organisation;

the nature of the organisation; and

other indicators such as the results of the analytical checks or other intelligence obtained in relation to the organisation.

If there is any significant concern that this could be the case, then little reliance, if any, should be placed on the company's internal controls. In this situation, an overall assessment of 'Low confidence' should be assigned. In this case, the appropriateness of the systems based audit excise audit approach for this company should be questioned.

Task 5 - Substantive testing (checking of records and transactions)

The aim of substantive testing is to obtain direct evidence as to the accuracy, completeness and authenticity of the company's records and physical stock or other holdings of interest to Customs / Revenue.

Design the tests to be applied

Substantive tests include inquiry, observation, inspection, confirmation, re-calculation and analytical review procedures. An example of a substantive test is whether receipts were correctly recorded and duty calculations were correct.

The auditor should establish which sub-system could result in material concerns to Customs / Revenue and devise a suitable test for each of these activities to either:

identify specific data processing (transaction) errors;

identify physical product on hand accounting errors; or

establish that records are within acceptable tolerances.

Tests could be based on complete verification of all activity/transaction occurrences or on the use of sampling techniques. If sampling is being used this may include

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stratification of the population of items to be checked so that testing is biased towards verification of the higher value or higher risk items.

Consideration should be given to the use of Computer Assisted Audit Techniques (CAATs) when determining the substantive testing approach to be taken.

Care must be taken to ensure that the prime computer records from Customs / Revenue's perspective are used.

The substantive tests (Test Details work-sheets AUD09) should be referenced back to the CAPE matrix work-sheets (AUD05) which identify the controls and potential errors that the substantive tests are intended to cover.

A typical audit test work sheet would include the following:

objective of the test;

description of the testing procedures;

level and extent of testing;

basis for sample selection and sample sizes and stratification definitions (if relevant);

and

the total sampling population.

Guidelines regarding the selection of sampling techniques to be used are provided.

Substantive testing sample size selection

Where sample testing is to be undertaken, it will be necessary to establish the extent of testing to be performed; that is the number of test cases to be checked for each test. This will depend on:

the overall level of 'audit risk' which the auditor is prepared to accept; and

the auditor's current level of confidence that the audit objective being verified by the substantive test has been achieved over the audit period. That level of confidence will be based on the preliminary assessments and control assessments performed in earlier stages of the audit.

The following outline provided a planning model expressing the general relationship of audit risk to the extent of reliance the auditor places on a substantive test of details, internal controls and other substantive tests, such as analytical review procedures, directed towards the assessment of the same specific control objective.

The model is:

Audit Risk = Inherent Risk X Control Risk X Detection Risk

where:

Inherent Risk is the auditor's assessment, based on knowledge of the company's business, transactions and practices, of the susceptibility of a class of transactions to error exceeding tolerable error before considering the operation of related internal controls.

Control risk is the auditor's assessment of the risk that error exceeding tolerable error that may occur will not be prevented or detected on a timely basis by the system of internal control. The assessment of this risk depends on the auditor's evaluation of

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the overall effectiveness of the internal controls relevant to the particular control objective. By evaluating the system and testing compliance with control procedures, the auditor assesses this risk for control procedures on which it is intended to rely in establishing the scope of the substantive test of details.

Detection Risk is the auditor's assessment of the risk that audit procedures (substantive tests of details) and analytical review or other substantive tests will fail to detect any remaining material errors.

In other words, the audit risk is a combination of the risk that material errors will occur and the risk that the auditor will not detect those material errors. This can be expressed in terms of a specified 'confidence level' that the auditor's assessment of the extent of possible error is correct.

Based on this audit risk model, the following table provides a guide to sample size selection where a high (that is in the order of 95%) overall confidence level is required:

Result of Initial Assessment (2/3/3)	Result of Control Assessment (2/5/5)	Substantive Testing Sampling Units (Items) to be Checked
Not using SBA	Not using SBA	200
Low or Medium	Low	200
Low	Medium	200
Low	High	100
Medium	Medium	150
Medium	High	50
High	Low	100
High	Medium	50
High	High	30

Note: If the population size is less than 2,000 then a *Finite Correction Factor* may be applied to reduce the sample size.

The above recommended sample sizes apply to manual processing and may be flexibly used. Sample sizes should be tailored to ensure that the audit objectives are adequately achieved.

Completing the substantive tests

The sample can now be selected from the total population based on sampling techniques. The substantive tests, which were previously designed, are now carried out. Any errors that are found should be documented on an Issues work-sheet (AUD 06).

If the sample size has been determined using the above table and no errors are detected, the auditor is able to reach a conclusion that with a confidence level of 95% no more than about 1.5% of the records in the total population being sampled are erroneous. There is a 5% chance that the actual number of records containing errors is more than 1.5% of the total population. The ability to relate the sample results to a

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monetary value depends on the nature of the population being sampled and the sampling technique used.

If any errors are found in the substantive tests performed, and these cannot be shown to be isolated cases due to special circumstances which are not likely to affect the rest of the records, then it must be assumed that there is an unacceptable error rate and further action will need to be considered. This is because the sample sizes in the table above have been determined on a 'discovery sampling' basis.

The main principle that must be understood when conducting these tests is that there is no acceptable error rate in relation to detected errors. It is also important to consider the material consequences of the errors when deciding on what follow up action is appropriate.

Where the substantive test results have highlighted errors that are, or could be, indicative of a significant problem relating to a major non-compliance issue, then further action will be required. The initial consideration could be increasing the sample size to the next highest sample on the substantive testing sample size chart, or possibly 100% depending upon the circumstances.

Evaluation of substantive test results

Possible further action - Accidental error:

In this case, if not determined to be isolated instances, the results of the audit will need to be discussed with the audit manager and a decision made concerning further action to be taken. This action would normally be a recommendation to the company to improve their compliance.

Any problems noted during the substantive testing stage of the audit will be brought to the company's attention and an Issue work-sheet (AUD 06) raised for inclusion in the audit report.

Possible further action - Suspected fraud

The above actions are based on an assessment that non-compliance is related to accidental error on the part of the company, or possibly fraudulent actions or theft by third parties against the company. The possibility of intentional evasion of duty payment by the company must also be considered when determining the appropriate course of action in relation to the findings of an audit.

If it is the assessment of the officer conducting the audit that the non-compliance detected may be due to fraudulent activity on the part of the company then this fact should be reported to the Compliance Team Manager immediately.

The Compliance Team Manager will then need to consider the need to recommend to the responsible areas such as Investigations that further action be taken.

Task 6 - Treating issues from the audit

Resolution of outstanding issues

At this stage of the audit, the audit working papers should contain the Issue work-sheets (AUD06) which document all of the issues identified during the conduct of the audit. Resolution of these issues will be recorded on the work-sheet. Issues will normally be resolved through a cooperative approach with the company.

Issue materiality assessment

Where issues are not resolved during the course of the audit, Issues work-sheets should be assessed by the audit team leader and Compliance Team Manager and each issue assigned a priority of either:

Major - the issue is considered to be one that the company must address and advise Customs / Revenue of the corrective action taken. These issues are expected to relate to the potential for significant non-compliance; or

Minor - the issue is considered to be one which either:

from the Customs / Revenue's perspective should be subject to tighter control but which is recognised as not posing a significant threat as the issue is not considered to be significant. While recommendations for improvement are made, the extent of corrective action taken would be at the discretion of company management under the principles of compliance improvement; or

is considered to be technically in breach of licence conditions or legislative requirements but is recognised as not being a matter that could lead to significant adverse consequences. The company would be expected to correct the situation to avoid the technical breach but would not be expected to advise Customs / Revenue of the action taken.

The priority is recorded in the top right hand corner of AUD 06.

Confirmation of issues

A meeting should be organised with the company's audit contact officer to discuss each of the issues identified. The aim of this meeting is to bring each of the issues and the priority assigned by Customs / Revenue team leader, to the attention of the company with a view to:

confirming that Customs / Revenue understanding of the issues is accurate and complete; and

where possible, establish a mutually acceptable course of action to address each of the issues.

A list of issues should be provided to the company audit contact officer at this meeting and an agreed timeframe established for responses to be received. There may be a need for follow up meetings with the company contact officer or other company staff to discuss specific issues. If necessary, these outstanding issues may be raised separately on a 'Follow-up Item' work-sheet (AUD07) with the relevant Issues work-sheet (AUD06) appropriately endorsed.

A cooperative approach should be encouraged at these meetings.

Task 7 - Reporting

The importance of audit reporting

The importance of this stage should not be underestimated since it is the primary communication from Customs / Revenue to the company executive. The work of the auditors will be largely judged by the quality and reliability of the audit reports.

Before the exit interview, the audit team should have prepared a draft Company Report (listing of recommendations and opinions) as a basis for the formal exit interview discussions. Following company comments/acceptance of Customs / Revenue's recommendations, the company's response is incorporated into the Company report. This finalised report is then given to the company.

The Internal Report will be compiled based upon the finalised Customs / Revenue Audit Report and the further detail of the audit including working papers.

In the case of less complex audits some of these steps may not be necessary as the bigger issues are most likely resolved during the meeting with company audit contact officer.

The auditor may modify the reporting format to suit the size and complexity of every audit.

Review of working papers

The final review of the working papers produced, the last of a series of reviews undertaken during the audit, should be undertaken by the audit manager before the issuing of the draft Company report.

The key matters requiring review and approval during the audit are as follows:
audit approach and audit program (timing - before audit field work commences);
CAPE matrix forms and substantive test plan (timing - before substantive test execution);
substantive test evaluation (timing - on completion of substantive testing);
issues sheets, including any risk categorisation of weaknesses (timing - prior to confirmation of issues with company audit contact officer);
final issue sheets and follow up item resolution and draft company report (timing - before the formal exit interview is held); and
final company report and internal report to Customs / Revenue management (timing - before issue/submission).

Review should take place at the conclusion of each phase of the audit, and a certain amount of review should occur while the work is being carried out. This allows for flexibility in amending testing procedures and documentation within the scope of the audit timetable. The reviewer should ensure that all work carried out is relevant to the aims of the assignment and evidence the review. Some tasks will be completed almost entirely in remote areas. In these circumstances, review will usually be by telephone discussion.

Customs / Revenue audit work may also be subject to independent Quality Assurance Review arranged senior management (see Section 6 of this manual).

Prepare draft company report

Reports to management should be prepared by the auditor in a manner that:
'Is clear, constructive and concise. The auditor would indicate the implications of all matters raised and, where necessary, use specific examples identified during the audit to illustrate the matter raised and assist the understanding of the user.'

A Company Report is raised at the conclusion of each audit.

This section does not deal with the style and quality of reporting but provides an indication of the matters that should be included in the report. The main contents of a typical report are noted at the end of this section.

The draft report should form a basis for discussion at the exit interview. It is important that this is held promptly at the completion of the fieldwork. This will enable Customs / Revenue and company management to focus on the major issues raised from the audit in a timely manner.

The auditor should report the implications of identified control absences or weaknesses in terms of the effect on Customs / Revenue's assessment of the achievement of the audit objectives. This should be supported, or balanced, by the results of the substantive testing performed where relevant.

The broad structure of a typical company report should be as follows:

Executive Summary - covering an introduction to the report, an overall assessment against the audit objective/s, a summary of the major issues being raised and notification of corrective action requirements, Customs / Revenue's expectations in relation to future notification of major change to systems and operational arrangements, and an acknowledgment in relation to the co-operation and assistance provided by company staff. The Executive summary would normally not be expected to be longer than two pages;

Contents page;

Appreciation of assistance given;

Introduction - covering the background to the audit, an overview of the relevant aspects of the company, the audit objectives and coverage;

Significant Audit Issues - covering each of the major findings of the audit in the form of an Observation section (what was found), an Customs / Revenue's concern section (why Customs / Revenue is raising the issue) and a Recommendations section (the corrective action required); and

Other Matters Noted - covering the minor findings of the audit in a similar but brief manner to the Significant Audit Issues coverage.

Review and endorsement of draft company report

A copy of the draft company report is to be provided to the Compliance Team Manager for review and endorsement prior to organising the exit meeting.

This review completed by the Compliance Team Manager is intended to ensure that the report is consistent with the quality expectations of Customs / Revenue's senior management and consistent with the goals of Customs / Revenue.

The Exit Interview

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At the conclusion of the fieldwork and after production and endorsement of the draft report, the exit interview will take place between Customs / Revenue and the company management. For most audits where there are significant findings, it is expected that at least the Compliance Team Manager and the auditor who led the assignment will attend the meeting.

The company will usually be represented by appropriate levels of management (including the audit contact officer).

The objectives of the exit interview phase of the audit are:
formal discussion with the company management to agree on the audit findings and to ensure they are aware of our assessment of their level of compliance;
formal discussions with company management to agree on any recommendations; and to enhance both the co-operative relationship and the goals of Customs / Revenue .
During the exit interview the company will be requested to reply to Customs / Revenue's recommendations indicating the action management has taken, or intends to take, as a result of the comments made in the report. This must be in writing within 14 days or such other period as your legislation / policy allows. This will provide evidence of company management's response to the issues raised, and form the basis for the comments included in the final company report. A copy of the company's response to recommendations should be filed with the audit working papers.

Issue final company report

Following the exit interview, and provision of a written response from the company management, the final company report should be produced.

The final report should ideally be issued within one month of completion of the fieldwork. In practice, this will usually be within 14 days of the exit interview (given that this interview will usually be within 14 days of the fieldwork).

The final report should include the draft report and include a 'Company Management Response' paragraph following each recommendation that documents the written response from company management.

The final report should be reviewed by, at least, the Compliance Team Manager before distribution.

Prepare and issue the internal Customs / Revenue report

The final activity to be performed in the conduct of a company audit is to prepare an internal report to management that covers:

Executive Summary - covering an introduction to the report, an overall assessment against the audit objective/s, a summary of the major issues being raised and notification of corrective action requirements, and an acknowledgment in relation to the cooperation and assistance provided by company staff. The Executive summary would normally not be expected to be longer than two pages;
an overview of the outcomes of the audit and details of any Customs / Revenue follow up activity required with the company;

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details of any issues arising from the audit which require further consideration/resolution within Customs / Revenue , for example in relation to policy matters or the interpretation of policy or legislation; and any issues relating to the need for further explanation, improvement or amendment to the excise audit methodology.

This report should be reviewed and approved by the Compliance Team Manager before issue.

Audit working papers and reports - Custody and classification

All audit working papers and reports should generally be accorded 'audit-in-confidence' status. Where one or more documents of a higher classification is included in the working papers or audit report, the file or report requires the higher classification.

Working Papers

Importance of working papers

The importance of complete, legible, well structured, indexed and adequately cross-referenced working papers cannot be over stressed.

Well-documented working papers for the audit are the physical evidence on which the auditor bases an opinion regarding the achievement of the audit objective.

Inadequate working papers expose the officer performing the audit, and Customs / Revenue, to:

the possible inability to pursue an audit finding due to the lack of adequate evidence to support the issue being raised;

increased difficulty in the performance of any subsequent audit activity due to the inability of staff performing this audit to be able to learn from the experience of the previous audit as documented in the working papers; and

criticism regarding professionalism and poor management.

Good working papers should:

facilitate planning;

control the audit;

provide accessible information;

aid the reviewer;

facilitate reporting; and

facilitate future investigations.

The characteristics of good working papers are:

systematic organisation (including indexing and cross-referencing);

completeness and accuracy;

clarity and understandability;

relevance; and

legibility and neatness (neat hand written working papers are all that is required).

The content of working papers

The working papers should contain a record of:

the planning of the audit;

all relevant discussions held with company staff and issues arising from these discussions;

all company documents copied as supporting evidence;

the documentation (narrative and flow-charts) of the relevant data and product flows and the related systems and procedural controls identification and assessments;

all observations made and the issues arising from these observations;

all analytical checks, compliance tests and substantive tests undertaken;

all findings noted during the audit;

all reports produced; and

anything else which is considered significant for the audit.

All working papers should contain the following information:

who prepared the working papers;

the date that they were prepared; and

a page number which refers to the index

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All copies of documents, extracts from manuals etc are to be annotated with the following information (this would usually be in the case of a document containing an error):

who provided it;

on what date;

if it is an extract, the source (file identifier, book or manual name etc); and

a page number which refers to the index.

All checks and tests are to be documented to provide details of:

what is being tested or checked, ie sufficient detail to enable the reader to clearly identify the test or check being performed.

when the test was conducted, ie the date.

how the items were selected, ie the sampling technique used and details regarding established or estimated population size, the sample size and sampling mechanism (eg the random numbers used, the sampling interval and start point used, or the block periods used).

what items were selected for testing with sufficient detail so that if necessary the item can be relocated;

what the relevant details were of the items being tested;

which items were in error; and

what the details of the errors were - these details would be recorded on an Issues work-sheet for further follow-up.

It should be kept in mind that if the company refutes or disputes the auditors' findings they will be reliant on the contents of their working papers, and the documentation of tests and checks especially, to support findings. If they are incomplete or inadequate, the auditors are at a severe disadvantage.

All tests performed must be documented, not just the errors. This is important so that others, eg supervisors, reviewers and external auditors, can make an independent judgement regarding the quality of the auditors' work. It is even more important as proof of what the auditors did should a problem surface after the audit has been completed. Provided that the auditors have done a thorough job and this is evidenced by their working papers they cannot be subject to unwarranted criticism.

The structure of working papers

The working papers are to be generally structured into the following sections:

Planning

This section is to contain the planning notes including the results of initial discussions with the Compliance Team Manager and other staff regarding any specific checks to be performed during the audit, the officers assigned to the audit and the work plan and timeframe for the audit;

Information gathering and system process documentation

This section is to include the information obtained during the 'information gathering' stage of the audit and any further information obtained during the conduct of the audit. System process documentation is also carried out.

Analytical checks and initial assessment;

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Documentation and control identification;
Control and Potential Error (CAPE) Matrix;
Compliance testing and control assessment;
Substantive testing;

Issue Section

This section should be used to record issues that are to be followed up during the audit. It provides a memory jogger for the officer conducting the audit. As issues are followed up and resolved, they should be documented on the Issues work-sheet (AUD06).

Follow-up item section

Issue work-sheets are to be cross-referenced to the index. Where issues are not resolved during the audit, they should be reflected in the follow-up action sheet (AUD07). The unresolved issues will form part of the report to the company. Details of the issues and the methodology for resolution should also be recorded in the appropriate file. It is possible that only one AUD07 may be needed to list the outstanding issues outlined in AUD06;

Draft company report, exit interview notes and company response and final assessment; and

Final Assessment, Exit Interview Notes and Reports.

If desirable, this section can be used for all correspondence, records of conversation with client, etc.

Retention of working papers

The working papers are part of the set of records retained by Customs / Revenue about a client.

On the completion of the company audit, the working papers are to be stored. The binder containing the working papers should be clearly labelled so that the year of the audit coverage is clearly visible.

It needs to be kept in mind that working papers contain information that must be kept in confidence. Accordingly, the documents should be kept under adequate security, and access only provided where appropriate and authorised.

Standard working papers

Creation of working papers

These standard working papers are provided as an aid to documenting the audit. Their use is not mandatory under auditing standards. Auditors are encouraged to use these working papers as a basis in creating their own audit documents. However, any auditor compiling their own documentation is reminded that the level of documentation requirements, which they are intended to satisfy, must be achieved.

Working papers may be created using office automation tools such as word processing, spreadsheet, flow-charting applications and specialized audit software. In this case, the indexing and cross-referencing requirements must still be achieved in relation to the print copy of the working papers that are placed in the working paper binder.

Audit Training and Capacity Building

Index of standard Customs / Revenue working papers
(Refer to Section 5/4 for proforma standard working papers.)

W/P

<u>Ref No</u>	<u>Description</u>
AUD01	Working Papers Index
AUD02	General Working Paper
AUD03	Flow-chart Work-sheet
AUD04	Control Description Work-sheet
AUD05	Control and Potential Error Matrix Work-sheet
AUD05a	Control Evaluation Work-sheet
AUD06	Issues Work-sheet
AUD06a	Status Memo Sheet
AUD07	Follow Up Item Work-sheet
AUD08	Sub System Summary Sheet
AUD09	Test Details
AUD010	Testing Work-sheet
AUD011	Quality Control Work-sheet

General information on Customs / Revenue working papers

All work-sheets have a number of facets in common.

At the top of each work-sheet, the auditor should fill in the company details and the title of the audit. These serve as useful identifying information for the working paper (W/P).

The index field at the bottom should also be completed. This field should give each working paper a unique identifier within the audit. In most situations, it would be customary to give the working paper an index based around the section of the audit the working paper belongs to, and consecutively numbered within this section.

The normal way of dividing the audit into sections is reflected by the headings on the Working Paper Index (AUD01). Each of these sections would receive an identifying letter, usually ranging from 'A' for the Planning details to 'J' for the Final Assessment, Exit Interview notes and Reports.

By dividing the working papers into these sections, it helps the auditor to add working papers in an early section without upsetting the numbering given to later sections, while still allowing for a simple consecutive numbering of working papers within the section. Within the working papers file, a divider may be used to separate the sections, and make it easier to find the working papers belonging to a particular section.

At the bottom of all working papers are two boxes for the auditor preparing the paper and the supervisor/manager reviewing it to initial and date. The auditor preparing the working paper should initial and date the appropriate box on first completing the working paper. If any details are added later, these amendments should be individually initialled and dated.

Working paper contents

AUD01 - Working papers index

This working paper is designed to go on top of the working paper file. A reference letter for each section should be noted when the auditor starts this section in the working papers.

Blank lines at the bottom can be used for other section headings not included on the Working Paper Index. For example, the auditor may decide to create a special section for a specific area of background information.

The detailed numbering for each section should be added on completion of a section or towards the end of the audit.

AUD02 - General working paper

The General Working Paper is to be used in situations where none of the specific work-sheets are suitable. For example, where a systems based approach has been rejected and the audit team has resorted to a transaction based approach, or it may be used for narrative descriptions of the system under review or interview notes.

Alternatively, word processing tools or lined pads may be used to generate these working papers.

AUD03 - Flow-chart work-sheet

The Flow-chart work-sheet is to be used, as the name suggests, for drawing flow-charts. With document flow-charts, it is common to divide the chart into the sections or departments which process the documents. The line labelled 'Department' would normally be used for the department or section names, and vertical lines used to separate them on the flow-chart.

Alternately, automated flow-charting tools may be used.

AUD04 - Control description work-sheet

This work-sheet is commonly used in a risk matrix approach. It is generally used to describe in more detail, the identified controls included on a CAPE Matrix work-sheet (AUD05).

A full description of the control is included in the first box (Description). This could be headed up by a short description of the control that will be used on other work-sheets that reference this control. Any parts of the system documentation, which help to describe the control, should be referenced in 'documentation' section of the reference box on the right.

If this control is included on other working papers, such as Risk Matrixes, Issues work-sheets etc the reference to these should be included here as well. It is probably best to note these references at the time the link is established rather than trying to find them later.

The auditor may assess this control at the time it is documented or after completion of various tests. This assessment should be included in the 'Assessment' box.

Audit Training and Capacity Building

Identified controls will be subjected to testing. References to the compliance test plans and results that relate to this control should be noted in the appropriate places and a brief summary of the test results included in the 'Test Result Summary' box.
AUD05 - Control and Potential Error (CAPE) Matrix.

The CAPE Matrix is central to the systems based audit. One of these matrices should be used for each group of risks (ie those that relate to a sub-system) in the audit. The auditor should start by filling in the details of the sub-system under review in the header fields on the work-sheet. Various risk lists should have been formulated early in the audit (either obtained from a standard model or derived for this audit). A brief description of each risk (or associated exposure) should be included in the appropriated boxes at the top of the matrix. The inherent risk of these exposures should be noted in the darker row immediately below - these would normally be categorised as H (high), M (medium) or L (low).

During an earlier stage of the audit, the system should have been documented and some actual controls identified - these should have been described on Control Description work-sheets (AUD04). Others may need to be described after considering the potential errors for this sub-system. A brief description of the identified controls should be included in the appropriate column of the matrix, along with the reference to the work-sheet on which they are described in detail (in the Reference column).

The main body of the matrix can then be filled in - these cells can be filled in as the identified controls are put in their column, or after all those have been filled in. With each identified control, the auditor should consider its impact on each of the potential errors, and whether it reduces the risk for that potential error.

It should be remembered that a control is a feature of a system that *prevents or detects* an error. If it does not do this, it is simply a process and not a control. A 'P' or 'D' is placed in the cell depending on whether it is a preventative or detective control for this exposure. The P or D is circled in cases where the identified control is a key control for reducing the risks of the exposure. The impact of each control in reducing the risk identified is also rated as S (strong), M (medium) or W (weak). After completing the body of the CAPE matrix, the auditor needs to assess each potential error to see whether the controls identified are adequate at reducing the risk to an acceptable level. This is noted in the appropriate row at the bottom of the matrix with an S (strong), M (medium) or W (weak) and the risk remaining should be assessed as H (high), M (medium) or L (low).

The controls which have been identified as key controls for an exposure would be the ones subject to further compliance testing - if this leads to any deficiencies being identified, the 'risk remaining' may need to be modified. Any potential errors where the risk remaining is higher than 'Low' are areas of potential deficiency and could be written up on issue sheets or recommendations noted directly in the reporting process. A CAPE Matrix is a method of determining a level of confidence in controls in a system. A 'strong' control indicates Customs / Revenue has high confidence in the procedure or test being examined ie the level of risk present is assessed as low.

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A Risk Analysis Matrix is a method of determining the level of risk. A *severe* level of Risk indicates Customs / Revenue has assessed the event as being considered as a combination of:

almost certain likelihood (the event is expected to occur); and

extreme consequence (an event leading to serious damage, disruption and/or breach of control).

This means the event is highly likely to cause serious damage/disruption/breach of control.

A *severe* level of risk is an unacceptable outcome and, therefore, must be subject to treatment to manage that risk. The expectation must be to minimise and eliminate risk (subject to cost) by reducing the likelihood of an event occurring, or its consequences, or both likelihood and consequence.

AUD05A - Control evaluation work-sheet

This work-sheet can be used in either Desirable Control approach or CAPE Matrix approach. The first section should contain the objective of the control. In answering the question 'What is the control doing to achieve specific goals of the system/sub-system?', reference should be made to the control description contained in AUD04. In some situations, the controls may be lacking or non-existent. The auditor, having knowledge of the business and legislative requirements, can use his/her judgement or previous audit experience with other companies in the same industry to identify a desirable control (section 2 of the work-sheet).

In the future, efficiency can be best achieved by developing an audit test package that will address testing and evaluation of common controls and legislative requirements in a particular industry. The observation section should contain control rating: good controls, adequate/inadequate controls or no controls. Results of compliance and/or substantive tests should be included in the 'findings'. Having the observation and finding sections completed, the auditor is now ready to prepare his/her recommendations.

AUD06 - Issues work-sheet

The Issues work-sheet should be used when significant issues arise during an audit. In some situations, copies of these work-sheets may be provided to the company contact officer for comment and could form the basis for discussions before the formal exit interview. These work-sheets should be filled in progressively as an issue is progressed from being logged, discussed and cleared.

When an issue is first identified, it should be described in detail in the 'Description' box. Any suggested recommendations to help solve this issue could also be included at this point. Where a written response is required from the company, it may be appropriate to issue a status memo sheet (AUD06a).

As the issue is progressed, further details are added to the appropriate boxes. When this issue is raised with company management for comment, this should be noted in the appropriate box, along with the date in the box on the right hand side. The nature of how it is issued (copy of this form, summary report of issues etc) and the company contact officer to whom it is given should be noted in this box, along with any other working paper references.

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When company management responds, a summary of their response should be noted in the appropriate box, the date noted and the working paper reference of the response documents (if any). Follow-up action and the closure of this issue should also be noted in a similar way.

AUD07 - Issues follow up action sheet

This document should be used for issues that are not resolved at the time of the audit. This will form part of the findings to be included in the final report.

AUD08 - Sub-system summary sheet.

This work-sheet is intended to provide an overview of the assessments of the controls for a particular sub-system. For example, the confidence levels from the CAPE Matrix can be summarised on this sheet. This will save effort in wading through individual working papers to get this information and will assist in the writing of summary information in the reporting process.

The title and a brief description of the sub system should be included in the box at the top. In cases of small audits, this may just be the system title and description.

An overall assessment should also be made of each sub system and this is noted in the box at the bottom of the work-sheet.

AUD09 - Test details

This work-sheet is used for documenting the test plans for actual controls identified during the course of the review. It can also be used for substantive test plans that may not relate to a specific control.

A brief description of the control to be tested should be included in the first box ('Control to Test') and a reference noted on the right as to where the control is described in more detail (this may be a Control Description work-sheet (AUD04)). In some situations, multiple controls could be tested with the same test. All the relevant controls and their references should be included in these boxes in this case.

Details of the tests to be applied to this control/s should then be described in the 'Test Description' box. A box has also been provided to assist with the calculation of sample sizes and any rough workings where appropriate.

On completion of the tests, a brief summary of the findings should be noted in the 'Summary of Test Findings' box. References to other working papers, such as the testing work-sheets and detailed test findings should be noted at the bottom of the work-sheet.

An overall summary of the test results indicating whether the control is effective, not effective or the auditor is still undecided, should also be noted at the bottom of the work-sheet. There is also space for a brief summary of the reasons if the auditor feels that this is necessary.

AUD010 - Testing work-sheet

This work-sheet is used for recording the details of transactions tested and the test outcomes.

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Sufficient details should be recorded to enable a reviewer to reach the same conclusion as the person who carried out the audit. If, for example, the test is to ensure that tariff items are correct, a list of the lodgement numbers and line numbers would be appropriate.

AUD011 - Quality control/supervisor review work-sheet

It is expected that at least one of these work-sheets will appear on all working paper files. All audits should be reviewed by the Compliance Team Manager at several points in the audit and this work-sheet records the details of these reviews (along with the reviewer's initials and date at the bottom of all work-sheets reviewed).

The 'reviewer's comments' area of this work-sheet is in free form indicating that its contents should be of a flexible nature and would depend on the nature of the review and its findings. Any actions, which result from this quality control review, should be noted in the right hand column.

Audit Training and Capacity Building

Proforma
AUD01

Client _____

Working Paper Index _____

Activity No. _____

Section	Ref
Planning	A
Information Gathering	B
Analytical Checks and Initial Assessment	C
Documentation and Control Identification	D
Control Model/Control and Potential Errors (CAPE) Matrix	E
Compliance Testing and Control Assessment	F
Substantive Testing	G
Items To Be Followed Up	H
Issues/Findings	I
Final Assessment, Exit Interview Notes and Reports	J
Client communications	K

Prepared	Reviewed		
/ /	/ /		

Audit Training and Capacity Building

AUD03

Client

System/Area

Flow-chart Work-sheet

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD04

Client **System/Area**

Control Description

Description:	WP References Documentation: Control Evaluation Sheets: Risk Matrices:
Preliminary assessment: (test result summary)	Associated Findings: Recommendations:
*Control should be listed on the relevant sub-system Risk Matrices (AUD05). Details of any compliance testing of this control should be endorsed on Test Details work-sheet (AUD09).	Test Details: Testing Sheets: Test Findings:

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD05a

Client: _____

System/Area: _____

Control Evaluation Work-sheet

Control Objective/Section:	Ratings/Risk L M H
Desirable Control/Question:	L M H Rely Not Rely Not Applicable
Observations:	Control Rating Good Controls (3) Adequate Controls No Controls (0)

Findings: _____

Recommendations: _____

References: Control Description:
Tests:
Issues:

Sub System Summary:

Prepared by	Reviewed by	Index
/ /	/ /	

Audit Training and Capacity Building

AUD06

Client

System/Area

Issues Work-sheet

Description:	Priority:	
	Logged	
	Issued	
	Response	
	Follow-up	
	Closed	

Status Memo:

Issued:

Response:

Follow-up:

Closed:

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD06a

Client:

System/Area:

STATUS MEMO

Query::
.....
.....
.....

Response:

Issued:

Response:

Follow-up:

Closed:

Issued by	Response by	Index

Audit Training and Capacity Building

AUD07

Client

System/Area

Follow Up Item Work-sheet

Description:

Status Memo:

Follow-up:

Assessment:

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD08

Client

System/Area

Sub System Summary Sheet

Sub-System:	
Control Objectives:	Assessment: Refs:
Overall Assessment:	

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD09

Client

System/Area

Test Details

Control to Test:	References:
------------------	-------------

Test Description:

Samples: size selection method period population size

Summary of Test Findings:

Testing Work-sheet Reference:
Test Findings Reference:
[Effective/Not Effective/Undecided]

Prepared by	Reviewed by	Index	
/ /	/ /		

Audit Training and Capacity Building

AUD11

Client

System/Area

Quality Control Work-sheet

Review Points (including WP ref.):

Action:

--	--

Prepared by	Reviewed by	Index	
/ /	/ /		

Computer Assisted Audit Techniques (CAATs)

Use of CAATs

When an audit is conducted in an electronic data processing (EDP) environment, the application of test procedures may require the auditor to adopt techniques that use the computer as an audit tool. The use of a computer during the conduct of an audit is known as using Computer Assisted Audit Techniques (CAATs).

Audit software

Audit software consists of computer programs used by the auditor as part of the audit procedures to process data of significance held by the client on their EDP systems. Where possible the use of 'Audit Command Language' ACL is used in CAATs.

Common applications for 'ACL'

The following are some recommended uses for ACL software during audit activity.

Stock/inventory

calculate total of customer balances;
calculate totals by product category;
select monetary units sample of inventory; Generate exception reports, including negative values, quantity or cost, extension errors, etc;
select items from perpetual stock records;
report transaction after period end;
prepare aged schedule of stock items;
report months of stock-on-hand from usage history; and
report variations between test counts and perpetual history.

Debtors/accounts receivable

calculate total of customer balances;
summarize to product balances or transactions;
select monetary unit samples of balances and transactions;
identify accounts with credit balances;
prepare aged customer analysis;
generate exception reports, including balances over the credit limit, unusual terms or limits, large balances, etc;
select sample of accounts for confirmation;
report transactions after period end;
report duplicates in a sequence of invoices;
identify breaks in sequences of invoices;
report slow-to-pay accounts; and
report inter-company transfers.

Creditors/accounts payable

(Relevant to Customs / Revenue related transactions)

calculate total of credit balances;
summarise to produce balances by creditor; Select monetary unit samples of balances or transactions; Identify accounts with debit balances; Prepare aged payables analysis; Generate exception reports, including aged invoices, large balances or amounts, etc;
report transactions after period end;
report duplicate payments;
report missing (payment) cheque numbers;
report unauthorised large payments;

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report payments made to accounts or addresses other than those registered in the supplier's ledger; and
report payments made after the due date.

Purchases

summarise transactions held by account debited;
select monetary unit sample of transactions;
generate exception reports, including refunds, high values, etc;
report transactions after period end; and
report duplicate items.

Sales

summarise transactions by account credited;
select transactions for manual inspection;
generate exception reports, including credit notes, high values, etc;
report transactions after period end; and
report duplicate items.

Audit Review

The role of the reviewer

The reviewer should perform reviews at the completion of the 'critical' stages of each audit, namely the:

- completion of the systems description;
- completion of the draft detailed audit plan;
- completion of the risk matrix;
- completion of the control assessment phase;
- completion of the substantive testing phase;
- preparation of issue work-sheet for discussion with company contact officer;
- completion of the draft company report; and
- completion of final company report and internal report to Customs / Revenue management.

The above task reviews would normally be completed by staff with different levels of experience eg manager to review the control assessment forms and team leader to review the systems description.

The main objectives of the reviews are to:

- ensure that the detailed audit plan is appropriate and realistic;
- ensure that the various stages have been properly completed and decisions ratified prior to the commencement of the next stage;
- check that the documentation is adequate to support the control assessment;
- consider whether all significant potential risks have been identified;
- check that related Information Technology systems controls (such as program change and data file access controls) have been properly identified where relevant; and
- agree that the compliance and substantive testing results support the evaluation.

Role of the Compliance Team Manager (CTM)

The CTM:

is responsible for the overall supervision of the audit and ensuring the quality of audit work undertaken;

- must be adequately trained and experienced to review and assess the adequacy of the audit activity to the standard expected by Customs / Revenue;
- must have a good working knowledge of the industry being audited and be familiar with the company being audited;

- where appropriate, should attend the opening and exit meetings/interviews and must resolve any significant issues which arise during the audit; and
- must formally review the audit work undertaken at the relevant key points during the audit and note the occurrence of these reviews in the working papers.

Role of the team leader

The audit team leader is responsible for the day to day on-site supervision of the audit and for the ongoing review of work performed by team members during the audit.

Audit Training and Capacity Building

The team leader is expected to have significant audit (including systems based audit) experience and to have a good working knowledge of the industry and an understanding of the operations of the company being audited.

The team leader will normally be expected to:

determine, in consultation with team members, whether a systems based or transaction based approach is to be used in the audit;

in consultation with team members, develop the audit plan;

establish the nature and extent of compliance and substantive testing to be performed;

ensure that the results of compliance and substantive testing are properly assessed and further action taken where needed;

actively participate in the field work and provide on-site guidance to less experienced staff; and

be the main focus of day to day liaison with the company contact officer

Appendix D2. Working paper example.

Example Working Papers – Assert Pty Ltd

This example shows the type of information to include in audit working papers. It may not be relevant to your situation. It has not been filed in a folder with A-J sections.

As an exercise, dissect these papers and place them into an audit folder divided into A to J sections. Cross reference as appropriate.

Audit Training and Capacity Building

Initial Audit Plan

Audit Training and Capacity Building

Letterhead

File No. S 97/10368

Initial Audit Plan – Assert Pty Ltd

Team Manager

The initial audit plan compiled by Peter Wilson a fair estimate of audit timeframe and the scope and focus of the audit is covered quite adequately.

Early research has indicated that a few tariff issues need to be sorted out. I have spoken to the Tariff chemist about a couple of classifications, however ultimately they need to be resolved by IDM.

Ian Jones made assurances over the phone that all cargoes must be entered or they will not leave the wharf. This is yet to be seen, and if this is the case, it raises the question of adjusting entries after cargoes have been out-turned.

Mr Jones also made comments about getting the papers together, which is of some concern as I would expect that all relevant documents should be available upon request.

The verification of values will be interesting because of the payments being made to DEEPCUT MINES accounts overseas. Mr Jones says that it will not be a problem.

Audit Training and Capacity Building

File No.
TRNG/10368

Audit plan and preliminary research, ASSERT PTY LTD

This company was selected as part of the national audit covering all aspects of the operations of DEEPCUT MINES Limited. The company's central branch dealing with all matters of taxation was contacted advising of the audit scope which includes Assert Pty Ltd. A copy of that letter is on the Hi- Fert audit file TRNG/10368.

Telephone contact has been made with Ian Jones, who is responsible for orders, chartering and Customs issues generally. The audit has been loosely arranged and then re-arranged at short notice on at least two occasions. Mr Jones advised on 26 June that the protocols pursued with DEEPCUT MINES's Taxation area did not take into account that this is hectic time of the year for the company and him personally, because of rural sowing / growth demands for fertiliser. Following discussion with the audit supervisor, it was firmly agreed to commence the audit on 28 July 2003.

I have sent a facsimile of the required shipments to Jones on 26 June 2003, together with a confirmation of audit dates, as per pages 4 & 5.

Audit objective

The audit will be to determine all areas of company interaction with Customs, and to assess the level of compliance on a risk assessed basis.

Audit period

The audit period is from May 1996 to May 2003. Any issues of material significance noted for this period will be followed through to current entries.

Scope

The following areas will be included in the audit scope:

- known history from any Customs data, previous audits etc
- knowledge of client business
- any system of internal control, including systems controls if relevant
- classification
- tariff advices
- valuation
- PWA's
- exports
- statistical issues

Research

In the period from May 1996 to May 2003, Assert have imported 220 lines of goods on 150 entries, with a Customs value of \$120,341,030.87, and a duty payment of just \$950.00. These lines have all been, prima facie, the type of goods expected to be imported by a major fertilizer distribution company-namely prepared fertilisers, trace elements etc etc. Only one line has been other than this type of product-an agricultural spreader.

The last audit on this company was performed in August 1991, which was conducted on a 100% basis. The only errors of significance were the detection of two instances of gross over valuation of goods, as freight deduction from CIF values was heavily

Audit Training and Capacity Building

miscalculated. This was attributed to broker error. However, this company would still be considered a low inherent risk.

There is only one (database) reference to Assert, where Customs has rated them a "...zero risk....as all commodities..... are duty free." This opinion is not shared by the current auditors, as there is some measure of risk in any importation, and there are risks other than revenue risk.

(The ?? database) contains only one reference to a tariff classification change in June 1990 from goods of 2833 to goods of 3823, with a duty adjustment of \$658.41.

Only two tariff advices have been issued to Assert directly, whilst five other T/As have been issued covering goods from companies supplying possibly the same or similar goods to Hi- Fert. T/As are held in Att 2.

Of the eight PWA's issued, as per Att.4, none are for any material issue, relating instead to matters such as change of first port, bill number and so on.

Sales tax is exempt on fertilizer, vide item 159 of the Schedule1 Exemptions

At present, there is no export reference within the EXIT system for Assert in its own write. However, exports, if any, are possibly handled by freight forwarder.

Issues to be addressed at audit

Control environment

The first consideration will be to determine the control environment governing entry compilation and the data upon which that is based. As only two brokers are used, the level of influence/discussion/control held by Assert governing issues such as tariff classification will be determined. Controls over determination of quantity for out-turn purposes, ensuring shipments are actually entered, and payment reconciliation to entered values will also be examined.

The usage of a systems based or substantive audit approach will be resolved from the control environment identified, but as with all importers, a substantive element of testing is to be included. As the importer has requested in advance the documents we wish to examine, a selection of shipments based on an inherent risk rating of high-medium has been made. This can be further reduced or expanded during the course of the audit. This selection has been added to those shipments chosen from known risk pointers.

Classification

Five queries have been identified from research pertaining to classification. These are outlined within Att.5. As the classification of these goods relies upon chemical industry terminology, considerable IDM will need to be produced to resolve these queries, and possible reference to an Customs chemist. It is unlikely any duty changes will take place, but these issues are material from a statistical viewpoint given the volumes involved.

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Valuation

Valuation remains a concern, again for statistical reasons, but as the last audit found significant errors in this area, it will remain a key audit issue, particularly the calculation and deduction of freight costs from the CIF value.

Unentered goods

It is hoped to incorporate some means of testing from a Assert shipping file back to an entry, to ensure that imported goods have been properly entered. A risk identified is possible oversight of entry requirement due to the single line-bulk nature/duty free status of these shipments.

Correctly entered volumes.

Entries will be checked back to out-turn reports, to ensure that an exact, rather than invoiced estimate quantity, is entered.

Exports

The matter of whether Assert are engaged in exportation will be raised during the initial interview, and any exports thus identified will be subject to audit scrutiny.

Other issues

The compliance improvement concept will be explained at this local level. The nature of Assert's current business operations will also be discussed, as part of the process of our industry education and awareness.

Resources and expected duration

Tony Kermit and myself will conduct the audit. At this stage, it is envisaged that audit activity will take 5 working days (assuming all documents requested are available), whilst follow up issues and write up may take a further two weeks. Some clarification may be required from the Tariff Chemist on technical issues.

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Systems Description

ASSERT PTY LTD – S???? AUDIT

Systems Description - Narrative

The description of Assert's systems was divided into two flowcharts; - The out-turn of product from the ship and the preparation of the entry for home consumption.

OUT-TURN

The production of the out-turn was considered material because of the manner in which the cargo is invoiced and discharged.

The invoice is for the total cargo which allows for optional discharge at ports depending upon the need at each plant when the ship is on the coast.

Cargo is lifted from the ship and dumped into hoppers from which trucks are loaded. The trucks proceed to the weighbridge where they are weighed and issued with a Weighbridge Docket. The load details are accumulated on a Weighbridge Tally Sheet.

These two documents are sent to the Assert plant where the details are input to an EXCEL spreadsheet which consolidates and totals each product discharged on the Discharge Port Totals report.

All three documents are sent to the Distribution Office at Keswick where the Ship Discharge Totals report (the out-turn) is produced as an EXCEL spreadsheet.

The main control in this system is the fact that the reports are compiled from base documents which are verified by the weighbridge operator. It is considered that the system produces an accurate out-turn. Any inaccuracies in entered quantities are caused by the inefficient use of the out-turn by the Assert and the broker.

ENTRY OF THE PRODUCT

Central to this system is another EXCEL spreadsheet.

Projected orders are input to the spreadsheet by Ian Jones, Supply Manager based on inventory requirements for the forthcoming year. As specific details of vessels come to hand, the spreadsheet is updated. The out-turn quantities are input after the details arrive from the Plant Managers and a reconciliation against the total invoiced quantity for all ports is carried out.

The Customs entries are compiled by the broker based on expected discharge quantities for each port. Entered and actual discharge quantities could vary substantially. In fact, a port could be left off the discharge program altogether, after the entries are lodged.

Audit Training and Capacity Building

The relevant documents are filed in two files, one being the main operations file for each ship and the other contains the entry, invoice and Bill of Lading. The filing of documents proved to be inconsistent and the filing system could not be relied upon.

A Foreign Currency Payment Requisition is raised for the payment of each invoice. This is sent to Treasury and payment is made 14 days after departure of the ship.

Control Environment

It became apparent during the walkthrough of the systems that entry of correct quantities was more by good luck than good judgement and that the filing of documents was inconsistent.

The systems contain controls which ensure;

- that quantities discharged are accurately recorded
- that the Distribution office is advised of the quantities

that quantities discharged are reconciled against invoiced quantities, and that goods are paid for.

These controls ensure that the company's assets are secure, however there is no comparison between the out-turned quantity and the entered quantity. Neither are amending entries lodged when final quantities discharged are known. This means that both quantities and values can be incorrect. The broker has not lodged Tariff Advices for the imported goods. Therefore there is no control over accuracy of entered tariff items.

Control Assessment

Because of the lack of internal controls which reduce errors which affect compliance with Customs requirements and the fact that exact quantities can not be entered prior to discharge, the **LIKELIHOOD** of errors is considered to be **HIGH**

Because of the fact that most lines imported by the company are subject to free rates, the **CONSEQUENCE** of errors is considered to be **LOW**

The control assessment is that there is a **MEDIUM** level of confidence that material errors will not occur.

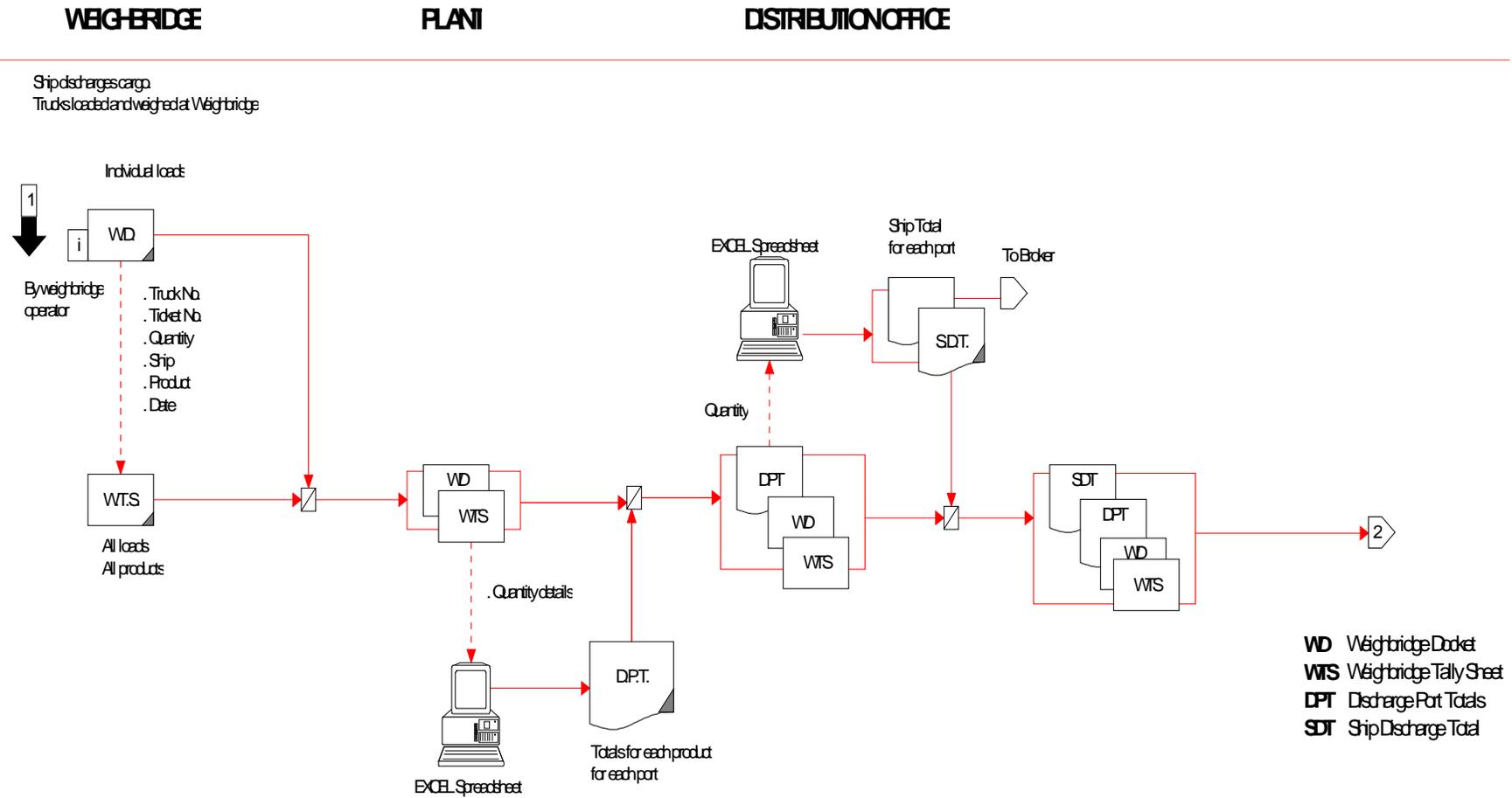
Audit Approach

This resulted in a decision that an audit which places an emphasis on internal control is inappropriate in this instance. A substantive approach will be followed.

Audit Training and Capacity Building

HFert Pty Ltd- Out-turn of Product

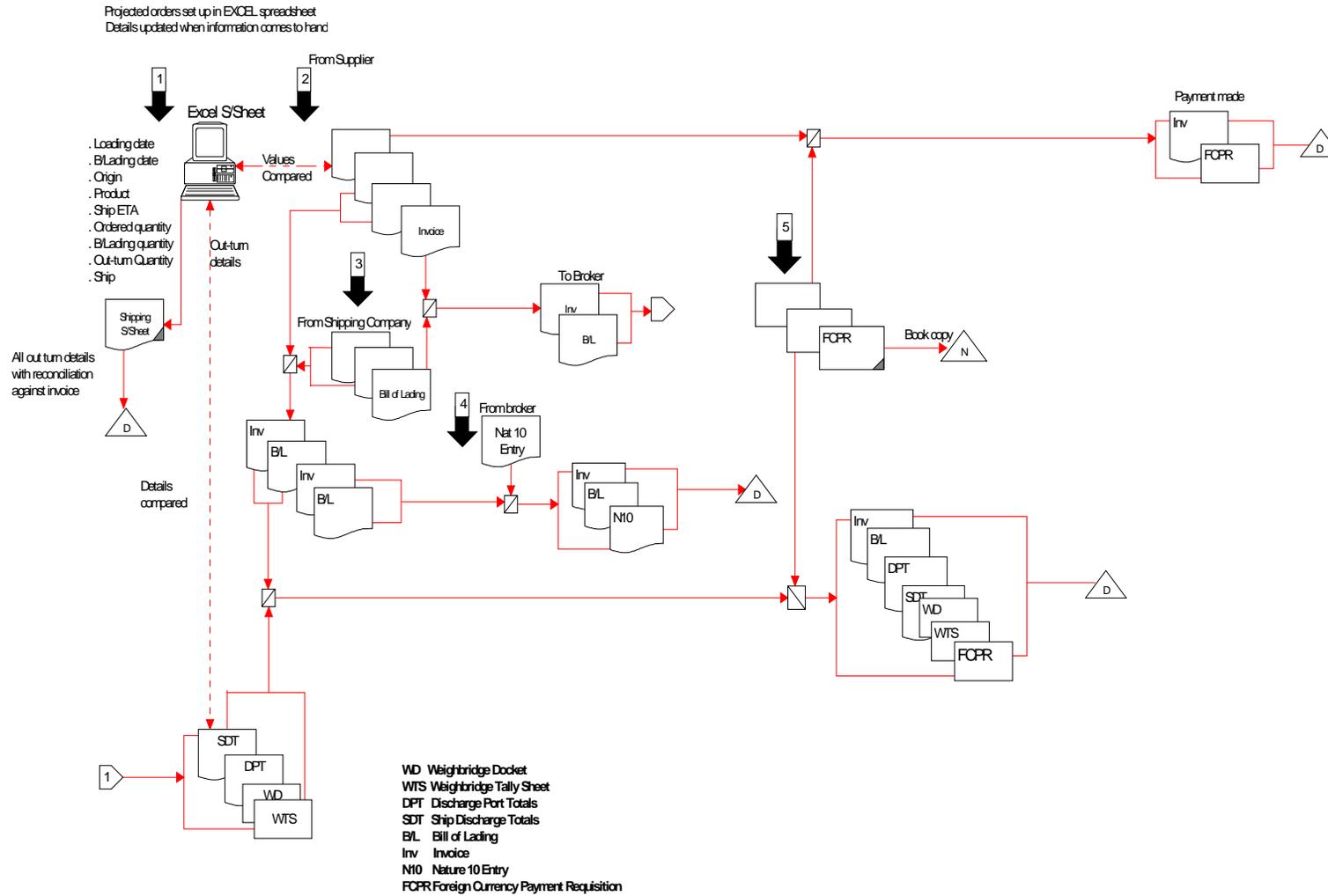
Flowchart 1



Hi-Fert Pty Ltd - Entry of Product
Audit Training and Capacity Building

Distribution Office

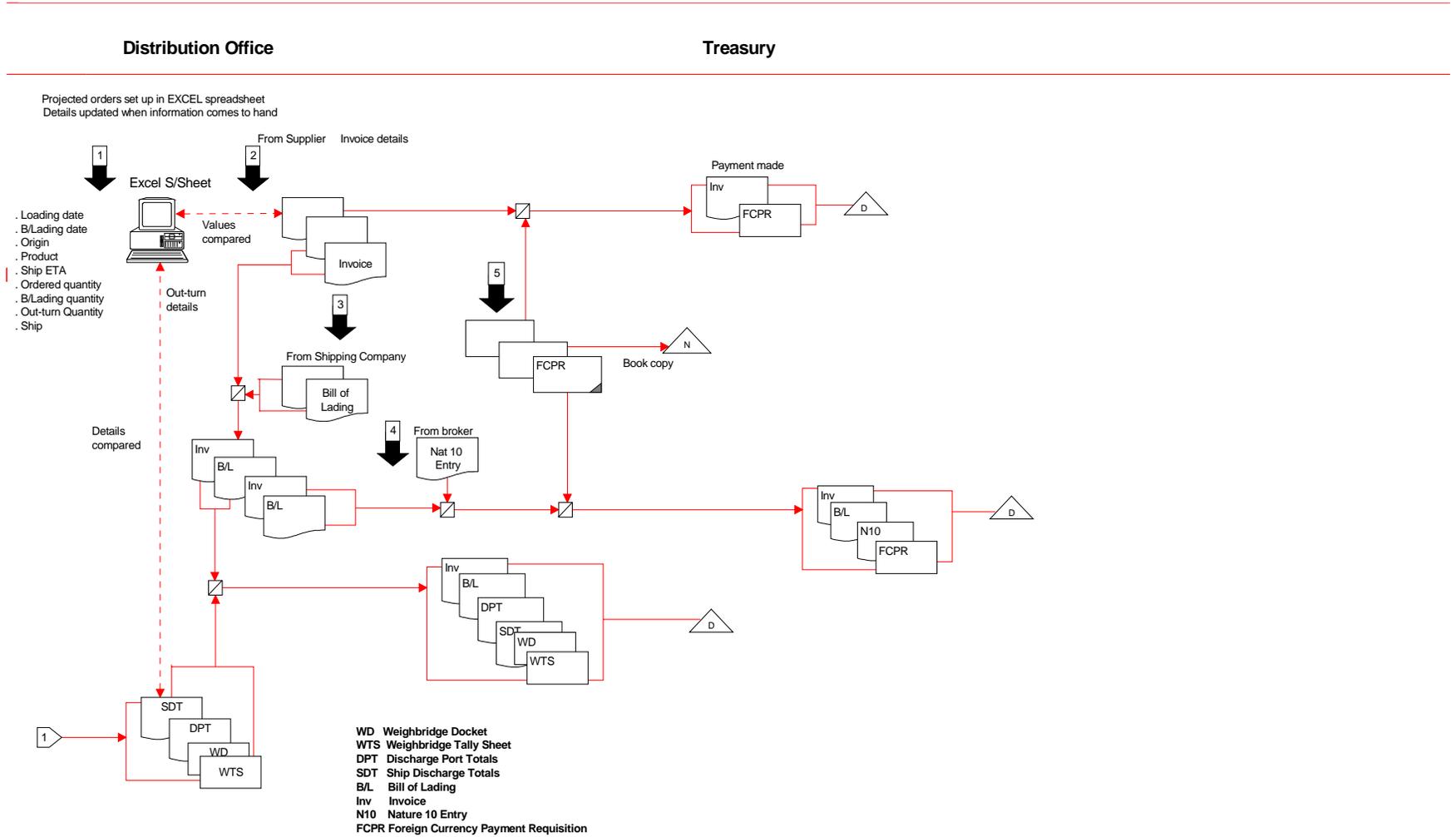
Treasury



Audit Training and Capacity Building

Hi-Fert Pty Ltd - Entry of of Product

Flowchart 2



Analytical checking and initial assessment

File No.
TRNG/10368

Analytical checking and initial assessment, ASSERT PTY LTD

Following provision of some descriptive company material, as per attachment 12, an attempt at a comparison of total tonnes of Assert fertiliser sales from the graph at page.....to fertiliser tonnes imported was considered. However, this comparison was abandoned when it was realised that volumes are added from local production, and an exchange relationship for imported product and local product exists with a Tasmanian manufacturer.

Graphing of entered imported tonnage trends was also considered and initial research undertaken, but a difficulty arose in that some bulk fertiliser components are recorded on entry in stat. units of kilograms (eg urea), whilst other are recorded in tonnes. Conversions for data purposes were undertaken, but a rather massive error was detected in 96/97 data for one entry which showed a broker conversion of the (approximate) 4000 tonnes actually off loaded into 4 billion kilograms. If this data had been accepted at face value for the purposes of analytical checking, it would therefore have included a volume of 4 million tonnes when it should have been 4,000 tonnes. A copy of the entry is at pages....&.....

Whilst no other errors were readily identified, the magnitude of this error was by itself material, and gave an indication that any other errors could be material not so much from their frequency, but from their potential dimensions, and that they could occur again. In addition, it could not be assumed that other broker conversions from smaller initial volumes were correct, and therefore, all things considered, the entered data could not be relied upon as a basis for analytical checking.

Consequently, analytical checking was discontinued. However, the exercise was not entirely pointless, as it showed the major error described above, which may have been missed in other forms of testing. A PWA will be required for this entry.

Substantive testing

File No.
TRNG/10368

Substantive testing, ASSERT PTY LTD

The importer's chartering manager, who has responsibility for Customs matters, requested advance notice of those documents which were to be subject to Customs examination. This request was reasonable given the client work pressures and for reasons of audit expediency, but it made a judgement of a justifiable sample difficult as at that point the control environment had not been identified and evaluated.

A decision was taken at that early stage to base the sampling on a high/medium confidence level, given the likelihood and consequence of potential errors, the past auditing history of the company, and the lack of any data at that point to suggest non-compliance.

Initial sampling population and unit

The population was taken to be entry lines for a the period May 1996 to May 2003, which numbered 220, and the sample adjustment formula for populations under 2000 was then applied, giving a sample size of 41 lines. A random number generator selected the sample from the database extraction at attachment 5. In addition, five classification queries identified from research were to be included with the sample.

Amended sampling procedure

During a walk through of the control environment, it became obvious that a proper sample would have to be selected around the vessel, rather than the individually entered lines chosen as per the preceding paragraph.

Because of the nature of bulk fertiliser, generally only two to four lines of goods are carried on a typical voyage. One invoice is usually held for each line for the total on board the vessel. Amounts to be off loaded at each port are not specified. Thus, any reconciliation of entry to invoice, bill, and outturn had to consider ALL of the entries covering all discharges of that line.

This aspect of substantive testing became critical when observation of the control environment, emphasised by flow charting, showed that a reconciliation between entered and outturned quantities did not take place. Thus, only a **MEDIUM** confidence level was held following the control assessment. See pagesto..... .

From the initial random listing as per folio5, four vessels were selected to examine all entries from those vessels at each port of call, in addition to the five shipments targeted from research. Whilst the population of entry lines was not particularly relevant for the reasons outlined, these four selected vessels effectively covered 69 of the 220 entries in the audit period, well above the required adjusted sample size of 41 for a **HIGH** initial assessment/**MEDIUM** control assessment.

Substantive test objective

The objective was to verify the veracity of data supplied on entry for home consumption and the revised sampling procedure of checking quantities discharged at all ports would have the benefit of providing some assurance that all goods discharged were entered.

Test description

(A) For those queries identified from research,

- obtain import file
- obtain separately filed broker's entry data
- check header details as follows:
 - invoice total
 - invoice terms
 - currency
 - port of discharge
- confirm correctness of classification
- verify valuation (payment) details

(B) For the four selected vessels for all ports of discharge,

- as above, and,
 - a total reconciliation of outturn volumes and entered volumes
 - a total reconciliation of all entered values to invoice

Substantive test results

For goods in category (A) test description, all files were located and all appropriate documents filed within, with the clearance documents filed separately as noted during the examination of the control system. Each of these queries related to products other than the main import lines (in volume terms) of GTSP (granular triple phosphate), MAP (monammonium phosphate), and DAP (diammonium phosphate).

Entered invoice terms for all of these goods were correct as entered, with containerised lines being CIF terms, whilst bulk cargo is on an FOB basis. For each of these shipments, a requisition of US\$ was sighted for DEEPCUT MINES's treasury area for payment which corresponded to invoice values, with a further separate requisition sighted for freight payment to charterers for FOB shipments.

Exceptions noted from substantive testing are as follows:

1) Goods variously described on entry as potassium nitrate, Multi K (potassium nitrate), Multi K Prills, from Haifa Chemicals of Israel, and entered to class. 28342100.

T/A10753500 (as per attachment 2) gives advice for goods described as

'Multi K fertiliser, being potassium nitrate (KN03), ratio 13-0-46, in 25 or 50kg bags for use as a fertiliser, supplier Haifa Chemicals'

as being proper to 31059000. IDM supplied by Assert for Haifa product (attachment 5A) describes the imported goods as

'Multi K' 'potassium nitrate (KN03) 13-0-46 prills' '....bagged in 50kg... or 25kg bags' 'Purity 97.6%'

Audit Training and Capacity Building

These goods are therefore considered identical to those of the T/A, and therefore these goods should be entered to 31059000. However, a further T/A, 12223900, (as per attachment 2B) issued for goods identified as

'potassium nitrate KNO₃, being 99.8% pure'

classifies these goods to 28342100, which is where Assert have been entering the prills from Haifa Chemicals. This issue has been referred to Tariff Section for a decision upon correct classification and application of Tariff Advice.

2) It was noted during research that amongst numerous lines of goods correctly entered to 31054000 as monammonium phosphate, there appeared three descriptions for monammonium sulphate, all for goods entered to either Port P or Port G. If goods were in fact of the latter description, they should be entered elsewhere. However, examination of documents for one of these shipments clearly showed all invoice, outturn and bill references to be for monamonnium phosphate. Consider NFA these lines, other than advice to importer.

3) For two shipments of goods described within database as "granusol manganese 28%", these have been entered to 38249090. As the 28% implies a mixture of some kind, IDM was requested to assist in confirmation of the claimed tariff item. The importer was unable to produce any at the time of audit. Research on the database system for any similar or identical product proved fruitless. This is comparatively only a minor line (and the only duty paying line), but the issue will be pursued with the importer.

For goods in category (B) test description. The four selected vessels were the *Vienna Wood* of May 1996, the *Lausanne* of June 1996, the *Vitkovice* of September 1996, and the *Bunga Orchid* of November 1996. These vessels carry the main bulk products imported by Assert, namely MAP, DAP, & GTSP, and visit 3 to 5 ports of call.

All of these vessels carried cargo on an FOB basis. Folders containing invoice, bill, freight invoice, port discharge totals, weighbridge totals, payment requisition etc, were compared to the separate folder containing entry copy, bill and invoice details. The classifications for all of these goods were considered correct against the details within the folders, and likewise the invoice terms. Payment requisitions to DEEPCUT MINES's treasury for the correct FOB invoice amounts were sighted for all shipments. Currently, the error margin between invoiced amounts and outturned amounts is negligible, so the invoiced value is what is remitted.

Significant errors were detected in entered volumes and values. The entries are compiled by an independent consultant, Peter Nemo, from data provided by Ian Jones. Nemo in turn engages the services of a broker, usually International Cargo Services, but occasionally Mayne Nickless to electronically lodge the entry.

To gain rapid clearance, an entry is lodged prior to vessel arrival at each port, with the best estimate available for the volume to be discharged included on the entry. These estimates can vary considerably to what is eventually unloaded, as store availability and orders can drastically effect the eventual outturn. The entered values are also based on the value per tonne of the estimated discharge.

Audit Training and Capacity Building

This process occurs for each port. No attempt is made by way of any amending entries to redress the incorrect volumes and values when total outturn is made for all ports of discharge. Indeed, there is no cross reference from entry to outturn performed in any capacity. Any PWA's lodged have been for incorrect vessel, port of discharge, bill number etc, but none for amending a volume or value. (see attachment 4).

The spreadsheets and graphs at pagestoshow the discrepancies in both entered volumes and values for this testing. All vessels showed errors, with the most significant being:

- an over entry of MAP of 2262 tonnes for the Vienna Wood, and an over valuation on entry of \$526,381.21. DAP shipped on this vessel showed only a marginal difference in volume entry to outturn, but the entered value was under-entered by \$262,096.28. The calculation of values per tonne were also incorrect due to anomalies between negotiated and the usual standard pricing.
- an over entry of 837 tonnes of DAP on the vessel Vitkovice, with a corresponding valuation over-entry of \$204,182.17.
- an over-entry of 1003 tonnes of DAP on the vessel Bunga Orchid, with a corresponding valuation over-entry of \$170,753.00

Lesser errors were recorded for the Lausanne and for instances other than the above, as per the spreadsheets, but the test showed that errors occur frequently, and that they can be of any magnitude.

Summary of substantive testing

- tariff classifications are acceptable, with two issues to be resolved by further IDM, and /or reference to Tariff branch.
- outturned volumes confirm volumes as per invoiced quantity
- payment documents confirm invoiced values and currencies
- entered invoice terms appear to be correct
- ports of discharge are correct, with all discharges checked being entered, however:
- the key finding of this audit is that entered volumes and values are generally in error when compared to invoiced and outturned volumes and values. This confirmed the control weakness identified in the control assessment.

VIENNA WOOD

ASSERT FILE REFERENCE

204

		Granular Triple Superphosphate (GTSP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1H.6134.0017H	1000.000	0.000	-1000.000	\$175,000.00
Port G	2G.6135.0006C	2500.000	3017.540	517.540	\$437,500.00
Port P	2P.6135.0001N	1500.000	2025.340	525.340	\$262,500.00
Port A	4A.6143.0099N	3300.000	3154.050	-145.950	\$577,500.00
Port W	4W.6143.0001P	600.000	420.540	-179.460	\$105,000.00
TOTALS		8900.000	8617.470	-282.530	\$1,557,500.00

Invoice	8900.000
Quantity	
Price / Tonne	\$175.00
Total Value	\$1,557,500.00
Difference	\$0.00

		Monoammonium Phosphate (MAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1H.6134.0017H	4000.000	643.380	-3356.620	\$878,000.00
Port G	2G.6135.0006C	7500.000	8478.160	978.160	\$1,646,250.00
Port P	2P.6135.0001N	1100.000	1573.120	473.120	\$241,450.00
Port A	4A.6143.0099N	2500.000	2416.540	-83.460	\$548,750.00
Port W	4W.6143.0001P	1200.000	926.380	-273.620	\$263,400.00
TOTALS		16300.000	14037.580	-2262.420	\$3,577,850.00

	TOTAL			
Invoice	6300.000	7714.697	14014.697	
Quantity				
Price / Tonne	\$237.00	\$202.00	\$217.73	
Total Value	\$1,493,100.00	\$1,558,368.79	\$3,051,468.79	
Difference		\$526,381.21		

		Diammonium Phosphate (DAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1H.6134.0017H	3000.000	3132.420	132.420	\$673,500.00
Port G	2G.6135.0006C	5000.000	4876.260	-123.740	\$1,122,500.00
Port P	2P.6135.0001N	1500.000	1619.160	119.160	\$336,750.00
Port A	4A.6143.0099N	3100.000	4062.440	962.440	\$695,950.00
Port W	4W.6143.0001P	4200.000	3135.740	-1064.260	\$942,900.00
TOTALS		16800.000	16826.020	26.020	\$3,771,600.00

	TOTAL			
Invoice	16200.000	547.325	16747.325	
Quantity				

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Price / Tonne	\$242.00	\$207.00	\$240.86
Total Value	\$3,920,400.00	\$113,296.28	\$4,033,696.28

Difference **(\$262,096.28)**

TOTAL ENTERED	\$8,906,950.00
TOTAL INVOICE/PAID	\$8,642,665.07
DISCREPANCY	\$264,284.93

LAUSANNE ASSERT FILE REFERENCE 211

		Granular Triple Superphosphate (GTSP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6169.0001K	0.000	0.000	0.000	\$0.00
	1N.6169.0002M	500.000	565.320	65.320	\$85,000.00
Port G	2G.6169.0005J	1700.000	1801.000	101.000	\$297,500.00
	2G.6169.0007M	2422.000	2302.000	-120.000	\$411,740.00
Port P	2P.6178.0001E	2300.000	2313.920	13.920	\$402,500.00
Port A	4A.6178.0016A	1000.000	884.740	-115.260	\$175,000.00
TOTALS		7922.000	7866.980	-55.020	\$1,371,740.00

			TOTAL	
Invoice	2921.936	4999.206	7921.142	
Quantity				
Price / Tonne	\$170.00	\$175.00	\$173.16	
Total Value	\$496,729.12	\$874,861.05	\$1,371,590.17	

Difference **\$149.83**

		Monoammonium Phosphate (MAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6169.0001K	3000.000	2786.400	-213.600	\$579,000.00
	1N.6169.0002M	0.000	0.000	0.000	\$0.00
Port G	2G.6169.0005J	2900.000	3014.000	114.000	\$559,700.00
	2G.6169.0007M	0.000	0.000	0.000	\$0.00
Port P	2P.6178.0001E	1500.000	1277.080	-222.920	\$289,500.00
Port A	4A.6178.0016A	700.000	1142.460	442.460	\$135,100.00
TOTALS		8100.000	8219.940	119.940	\$1,563,300.00

Invoice		8232.242	
Quantity			
Price / Tonne		\$193.00	
Total Value		\$1,588,822.71	
Difference		(\$25,522.71)	

		Diammonium Phosphate (DAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6169.0001K	7000.000	4049.160	-2950.840	\$1,386,000.00
	1N.6169.0002M	0.000	0.000	0.000	
Port G	2G.6169.0005J	6900.000	6005.800	-894.200	\$1,366,200.00
	2G.6169.0007M	0.000	0.000	0.000	
Port P	2P.6178.0001E	1500.000	1705.750	205.750	\$297,000.00
Port A	4A.6178.0016A	4300.000	7716.260	3416.260	\$851,400.00
TOTALS		19700.000	19476.970	-223.030	\$3,900,600.00

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Invoice		19508.345
Quantity		
Price / Tonne		<u>\$198.00</u>
Total Value		<u>\$3,862,652.31</u>
Difference	\$37,947.69	
	TOTAL ENTERED	<u>\$6,835,640.00</u>
	TOTAL INVOICE/PAID	<u>\$6,823,065.19</u>
	DISCREPANCY	<u>\$12,574.81</u>

BUNGA ORCHID ASSERT FILE REFERENCE 237

		Granular Triple Superphosphate (GTSP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6323.0020D	4500.000	4579.200	79.200	\$821,250.00
Port D	6D.6323.0003D	500.000	552.760	52.760	\$91,250.00
Port G	2G.6327.0002H	4500.000	4499.860	-0.140	\$821,250.00
Port P	2P.6344.0001C	0.000	0.000	0.000	\$0.00
	2P.6327.0001H	5700.000	5204.360	-495.640	\$1,040,250.00
Port A	4A.6331.0131B	3832.000	3979.920	147.920	\$699,340.00
Port W	4W.6331.0001M	300.000	426.100	126.100	\$54,750.00
TOTALS		19332.000	19242.200	-89.800	\$3,528,090.00

Invoice 19381.797
 Quantity
 Price / Tonne \$182.50
 Total Value \$3,537,177.95
 Difference **(\$9,087.95)**

		Monoammonium Phosphate (MAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6323.0020D	0.000	0.000	0.000	\$0.00
Port D	6D.6323.0003D	0.000	0.000	0.000	\$0.00
Port G	2G.6327.0002H	600.000	643.140	43.140	\$119,550.00
Port P	2P.6344.0001C	100.000	94.380	-5.620	\$19,925.00
	2P.6327.0001H	0.000	0.000	0.000	\$0.00
Port A	4A.6331.0131B	1750.000	1687.110	-62.890	\$348,687.50
Port W	4W.6331.0001M	1810.000	1710.000	-100.000	\$360,642.50
TOTALS		4260.000	4134.630	-125.370	\$848,805.00

Invoice 4150.594
 Quantity
 Price / Tonne \$199.25
 Total Value \$827,005.85
 Difference **\$21,799.15**

		Diammonium Phosphate (DAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6323.0020D	2000.000	1406.220	-593.780	\$408,500.00
Port D	6D.6323.0003D	6000.000	5902.760	-97.240	\$1,225,500.00
Port G	2G.6327.0002H	3200.000	3173.780	-26.220	\$653,600.00
Port P	2P.6344.0001C	0.000	0.000	0.000	\$0.00
	2P.6327.0001H	0.000	0.000	0.000	\$0.00
Port A	4A.6331.0131B	3500.000	3377.360	-122.640	\$714,875.00
Port W	4W.6331.0001M	4610.000	4446.880	-163.120	\$941,592.50

Audit Training and Capacity Building

TOTALS		19310.000	18307.000	-1003.000	\$3,944,067.50

Invoice		18474.000
Quantity		
Price / Tonne		\$204.25
Total Value		<u>\$3,773,314.50</u>
Difference	\$170,753.00	

TOTAL ENTERED	<u>\$8,320,962.50</u>
TOTAL INVOICE/PAID	<u>\$8,137,498.31</u>
DISCREPANCY	\$183,464.19

VITKOVICE ASSERT FILE REFERENCE 225

		Granular Triple Superphosphate (GTSP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6236.0007N	2500.000	2723.060	223.060	\$436,250.00
Port D	6D.6236.0002H	2000.000	1975.900	-24.100	\$349,000.00
Port P	2P.6242.0004P	3100.000	3099.000	-1.000	\$543,950.00
Port A	4A.6242.0041E	4700.000	4499.070	-200.930	\$820,150.00
Port L	4L.6242.0001E	1500.000	1752.750	252.750	\$261,750.00
TOTALS		13800.000	14049.780	249.780	\$2,411,100.00

Invoice	13997.343
Quantity	
Price / Tonne	\$174.50
Total Value	<u>\$2,442,536.35</u>
Difference	(\$31,436.35)

		Monoammonium Phosphate (MAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6236.0007N	0.000	0.000	0.000	\$0.00
Port D	6D.6236.0002H	0.000	0.000	0.000	\$0.00
Port P	2P.6242.0004P	0.000	0.000	0.000	\$0.00
Port A	4A.6242.0041E	2500.000	2499.990	-0.010	\$518,125.00
Port L	4L.6242.0001E	3000.000	2974.250	-25.750	\$621,750.00
TOTALS		5500.000	5474.240	-25.760	\$1,139,875.00

Invoice	5498.273
Quantity	
Price / Tonne	\$207.25
Total Value	<u>\$1,139,517.08</u>
Difference	\$357.92

		Diammonium Phosphate (DAP)			FOB \$US
PORTS	Entry	Entered	Out Turn	Variance	Value
Port N	1N.6236.0007N	1000.000	1005.780	5.780	\$212,250.00
Port D	6D.6236.0002H	5000.000	4001.900	-998.100	\$1,061,250.00
Port P	2P.6242.0004P	3900.000	3841.880	-58.120	\$827,775.00
Port A	4A.6242.0041E	0.000	0.000	0.000	\$0.00
Port L	4L.6242.0001E	8100.000	8313.000	213.000	\$1,719,225.00
TOTALS		18000.000	17162.560	-837.440	\$3,820,500.00

Invoice	17038.011
Quantity	
Price / Tonne	\$212.25

Audit Training and Capacity Building

Total Value
Difference

\$204,182.17

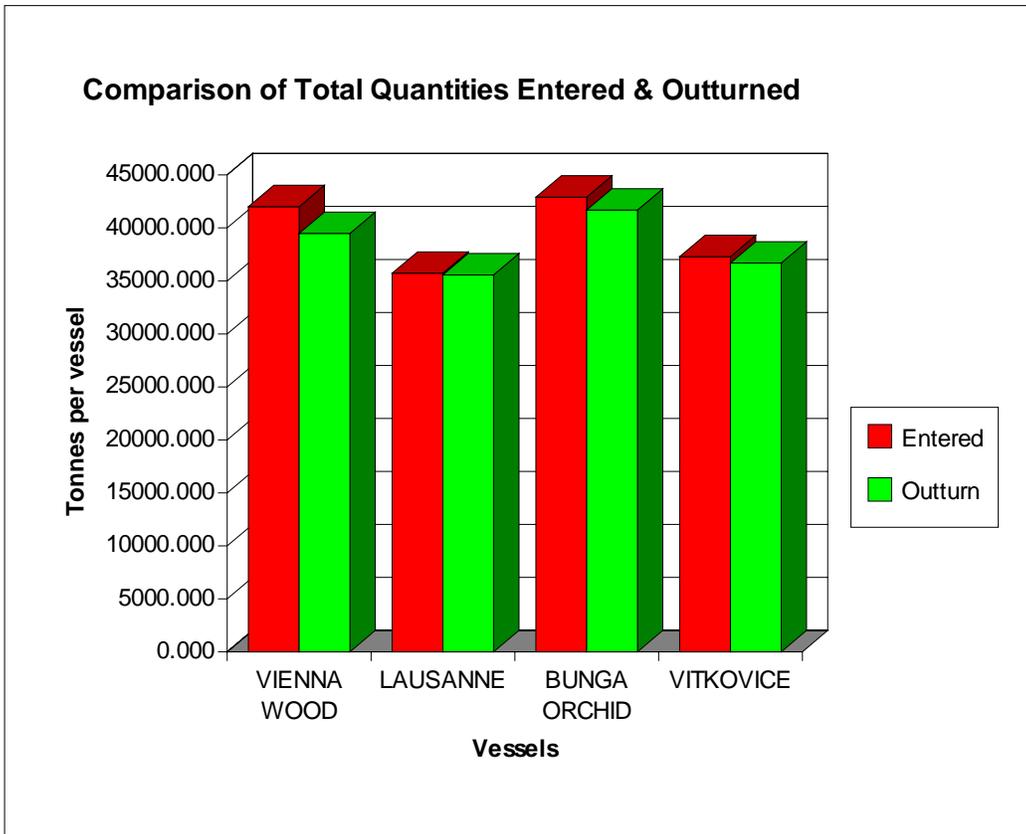
\$3,616,317.83

TOTAL ENTERED
TOTAL INVOICE/PAID
DISCREPANCY

\$7,371,475.00

\$7,198,371.27

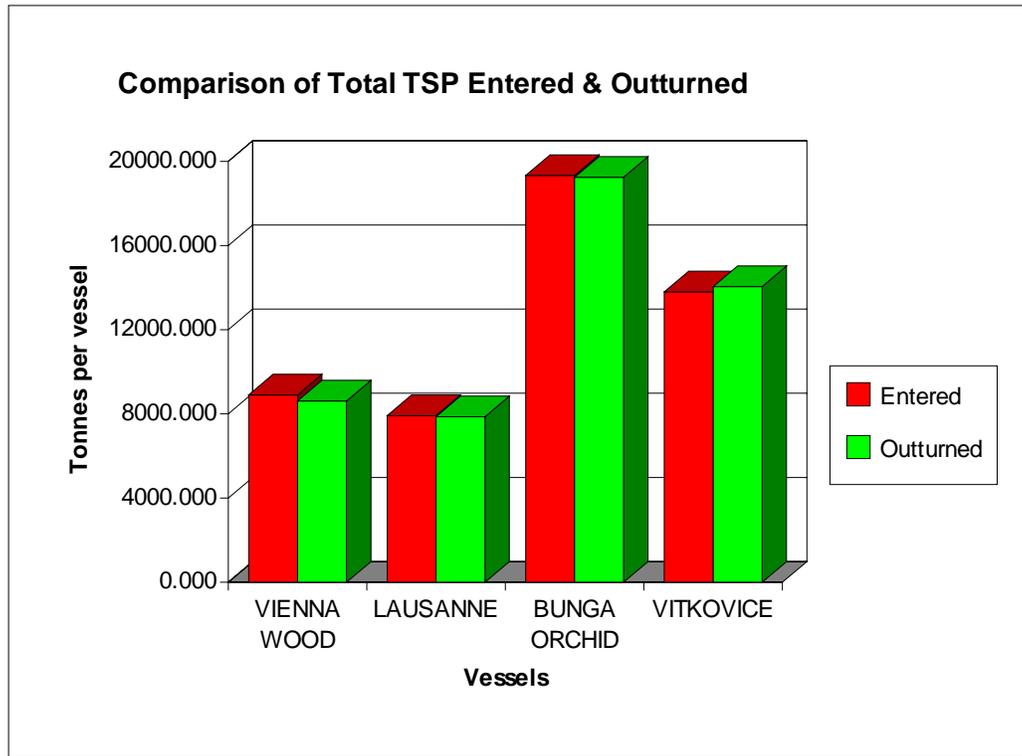
\$173,103.73



Audit Training and Capacity Building

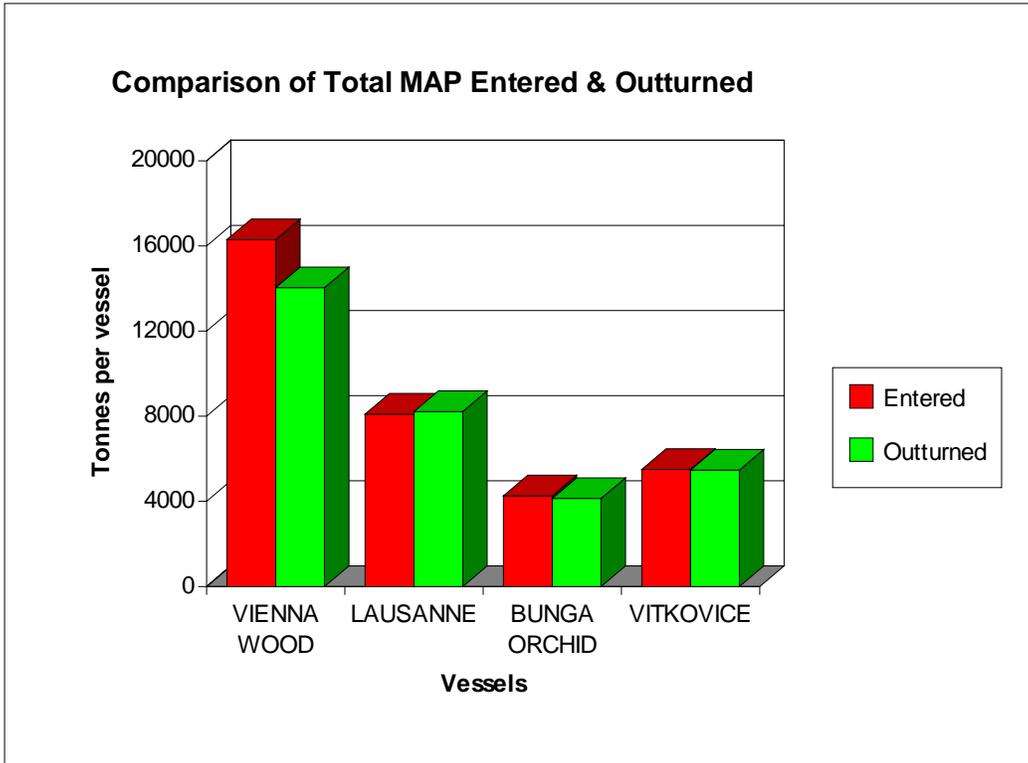
	TOTAL ENTERED (Tonnes)	TOTAL OUTTURNED (Tonnes)	VARIANCE (Tonnes)
Port N	28500.000	20890.940	7609.060
Port G	37222.000	37811.540	-589.540
Port D	13500.000	12433.320	1066.680
Port P	22200.000	22753.990	-553.990
Port A	31182.000	35419.940	-4237.940
Port W	12720.000	11065.640	1654.360
Port L	12600.000	13040.000	-440.000

Granular Triple Superphosphate (GTSP)



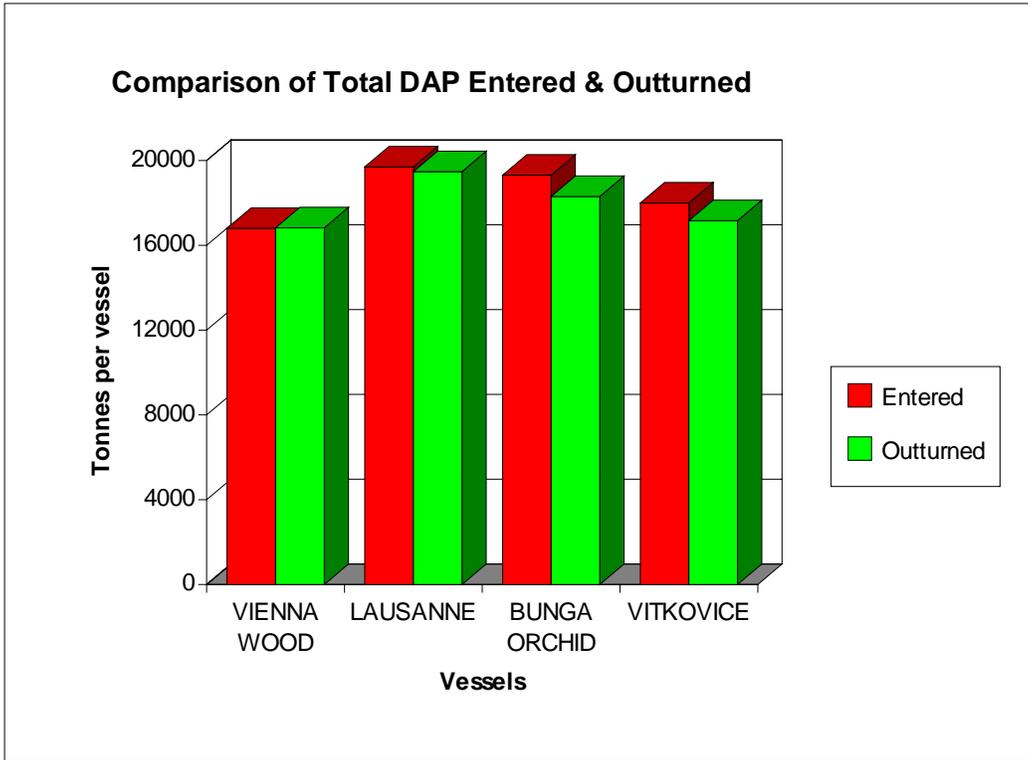
	Entered	Outturned	Variance
Vienna Wood	8900.000	8617.470	282.530
Lausanne	7922.000	7866.980	55.020
Bunga Orchid	19332.000	19242.200	89.800
Vitkovice	13800.000	14049.780	-249.780
TOTALS	49954.000	49776.430	177.570

Monoammonium Phosphate (MAP)



	Entered	Outturned	Variance
Vienna Wood	16300.000	14037.580	2262.420
Lausanne	8100.000	8219.940	-119.940
Bunga Orchid	4260.000	4134.630	125.370
Vitkovice	5500.000	5474.240	25.760
TOTALS	34160.000	31866.390	2293.610

Diammonium Phosphate (DAP)



	Entered	Outturned	Variance
Vienna Wood	16800.000	16826.020	-26.020
Lausanne	19700.000	19476.970	223.030
Bunga Orchid	19310.000	18307.000	1003.000
Vitkovice	18000.000	17162.560	837.440
TOTALS	73810.000	71772.550	2037.450

Audit Training and Capacity Building

Audit Issues

File No.
TRNG/10368

Audit Issues, ASSERT PTY LTD

Whilst outturn quantities have proven to be close to the invoiced volumes, the key finding of the audit is the inaccuracy of entered volumes and values against invoice values and outturned quantities. Because of the nature of these bulk fertilisers, entered volumes and values are an estimate only, but no amending entries are lodged to rectify these inaccuracies. The auditors have found that there is in fact no final check procedure by either the owner, consultant or broker to reconcile what was in fact off-loaded to what was entered.

This lack of a final check procedure also means that errors such as the conversion of tonnes to kilograms for entry quantity purposes also go unchecked. Thus, errors occur with considerable frequency, and can be of any magnitude, as exemplified by the error discovered during analytical checking (refer pages.....&.....)

These errors are endemic, and will continue to occur unless change is implemented. Over time, they have the capacity to upset statistical records of fertiliser importations, both in total overall tonnages and values, and in discharges at individual ports. For this reason they are considered material errors.

The importer's representative, Ian Jones, and the consultant, Peter Nemo, acknowledged the problem when the issue was discussed on the 26th of August. They outlined the need to lodge an advance entry to rapidly clear the goods, but that sometimes they will not know the volume to be discharged until loading has finished, as storage space considerations, manufacturing needs etc constantly impact upon what is eventually discharged.

Ideally, from our point of view, amending entries should be lodged for each product and port of discharge where any significant error has occurred in entry. This could in reality mean up to 21 amending entries for one vessel. This is not a particularly facilitative solution. Nemo claims that 40AA permissions were once used, but Customs had ended this due to some problems in Port G some years ago.

It was suggested by the auditors that Nemo may wish to take up the issue with the manager of Industry Services & Trade Facilitation to see if a more workable solution can be found. To date (13th August), this has not been pursued by Nemo. It was the audit teams opinion that there is some reluctance on the part of both Nemo and Jones to change anything in their procedures. From their point of view, their methods ensure that the ordered goods are delivered in total by good outturn procedures, and there is no real problem for Customs as the goods are duty free.

It was pointed out that whilst there are no revenue concerns, the issue of statistical correctness is an important one from a trade point of view.

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At this point, a retype is considered appropriate for the over-entered 4 million tonne urea cargo, and, taking into account any opinion or decision from our (specialist) area, a letter including concerns over entry accuracy and a means of resolving the problem to Customs satisfaction will be forwarded to Assert.

Audit Training and Capacity Building

Draft Advice to Client

Letterhead

14 August 2003

Assert Pty Ltd
Attn: Mr B Garbellini
Address

cc Mr P Nemo

Re: Customs Compliance Audit, July 2003

Dear Sir

I refer to the recent Customs compliance audit conducted at your premises on the 28th and 29th of July 2003. I would like to take this opportunity to thank Mr Ian Jones of your company for the high level of co-operation and assistance received during the audit.

The main issues arising from the audit are as follows:

Classification

Customs is generally satisfied with the correctness of the classifications within the terms of the Customs tariff. One issue which could not be resolved during the audit was the classification of a product entered as "granusol manganese 28%", imported from Tennant Ltd. In order to confirm the claimed classification of 38249090, further descriptive material is requested which details the contents and description of this product.

Entered volumes and values for bulk shipments

Whilst the audit determined that very good controls exist for confirmation of invoiced volumes against outturned volumes for bulk fertiliser importations, it was noted that the volumes and values entered for Customs purposes on Customs entries are estimates only, and that large discrepancies can exist between the Customs entry and what was actually received on outturn.

As an example of this concern, the *Vienna Wood* of May 1996 had an over-entered quantity of MAP of 2262 tonnes, and an over-valuation on entry of \$526,381.21 for this line. DAP on this vessel, whilst being reasonable in terms of quantity, was under-entered by \$262,096.28.

An examination of control procedures governing correct entry found that there is no formal procedure in place to determine the correctness of Customs entries against what is eventually outturned. This means that errors of any magnitude will go undetected. An example of this is on the enclosed copy of entry 4A62420030B, for urea carried on the vessel *Western Condor* in August 1996. The invoice quantity as entered (which is what the data system reads as the imported quantity) has been recorded as 4 billion kilograms or 4 million tonnes. Collectively, errors such as these have the capacity to effect the compilation of accurate trade statistics.

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In this particular instance, an amending entry is required to correct the entry referred to above.

Customs appreciates that the nature of Assert's cargoes and the requirement for rapid clearance results in a forward estimate entry for each port of discharge, and that commercial realities are that these entered quantities and values may not be reflected in what was actually discharged. To this end, your consultant for Customs clearances (Peter Nemo) has already commenced discussions with Customs Industry Services & Trade Facilitation branch to explore means of more accurate Customs entries with due consideration given to the requirements of trade facilitation.

The implementation of a control is suggested by which the Customs entries are checked for the accuracy of the entered values and quantities against the volumes outturned, and, dependent upon the outcome of the discussions, a process is developed to ensure that any significant discrepancies on those entries are properly adjusted.

Customs looks forward to the early resolution of the issues identified during the audit. If you have any queries, please contact either myself on 84479400, or Peter Bardsley on 84479209.

Yours faithfully

(A D Kermit)
(Title etc)

Audit Training and Capacity Building

Audit Report

AUDIT REPORT
COMPLIANCE AUDIT - ASSERT PTY LTD
A DIVISION OF DEEPCUT MINES

Manager

The Assert compliance audit has now been completed. The audit was conducted as a part of the national audit of Deepcut Mines.

Audit Staff

The audit was conducted by:

Tony Kermit	Audit team leader
Peter Brady	Senior auditor
Nick Jeanluc	Auditor

At the commencement of this audit, it was established that the risk consequences were small in the revenue area. The risk for statistical accuracy was considered to have higher consequences due to the entry of bulk cargoes and the entry prior to the out-turn of the cargo.

Audit Scope

Import of fertiliser and associated chemicals is the only relationship which Assert has with the Customs and therefore the scope of the audit was the importation of goods. The company does not export.

Audit Focus

The focus of the audit was particularly the correct entry of quantities and values of bulk cargoes. Tariff classification was also covered.

Audit issues

The issues which arose during the audit and their resolution are listed hereunder.

- **Classification of multi-k prills**

The production of IDM showed that the goods are being correctly entered.

- **Classification of granusol manganese**

This will be followed up with the company in the exit letter as specifications are still to be supplied by the exporter.

.../2.

2.

- **Out-turn of product and entry for home consumption.**

OUT-TURN

This is a critical document and has strong controls over its preparation. Audit opinion is that the quantities reported on out-turns for each port are correct.

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ENTRIES

Entries for home consumption do not reflect these accurate quantities. This comes about because of the nature of these bulk cargoes, the fact that intended quantities for each port can change and the lack of a detective control of comparison of out-turn with entries within the importer's systems.

The possible options for remedial action are giving permission for delivery without entry with exact entry after out-turn, or the entry of approximate quantities with amending entries after out-turn.

As this is a processing matter, it is being followed up by (???) and therefore the issue is resolved as far as this audit is concerned.

- **Exit interview**

The exit interview letter with recommendations and issues which require subsequent follow-up is herewith. An interview will be arranged in due course.

- **Overall audit assessment**

The overall audit assessment can be expressed as a MEDIUM level of confidence that compliance will be at acceptable levels in the future. This is based on the fact that the consequences of errors in the future are low to medium whilst the likelihood is medium to high. The future level of compliance is ultimately dependant upon the outcome of negotiations between the client and ??? with regard to the accurate entry of bulk cargoes. The audit team has no influence over the outcome of these discussions

Audit Training and Capacity Building

Audit Team Leader
14/8/03

File No.
TRNG10368

Senior Compliance Officer T Kermit
Compliance Officer N Jeanluc

Assert Pty Ltd Outcome of issues arising from July/ August 2003 Audit.

In response to our audit letter at folios 11 &12, Assert and their consultant Peter Nemo, have moved quickly to resolve the audit issues identified in the letter. It appears as though Dean Lambert has been retained as a further consultant for some or all of these issues.

- A PWA (as per folio 18) has been lodged to amend the grossly over-entered urea shipment on the vessel Western Condor.
- IDM (folio 16 & 17) has been submitted, as requested, for granusol manganese. Tariff have informally accepted these goods as correctly entered to 38249090.
- The main issue, that of correct entry of discharged volumes and value for the bulk fertiliser shipments, has been taken up by our ISTF area (K Branson), and a workable procedure has been devised. However, the whole issue of the need for accurate entry data versus reasonable facilitation for bulk cargo has been referred to ISTF's policy area in central office. File TRNG/01230 covers this aspect of Asserts interaction with Customs.

Consequently, should Assert maintain their intentions in line with the above initiatives, they can be rated a minimal risk in future audit considerations.

P Brady
Compliance Officer
Industry Group #1

Audit Training and Capacity Building

26 August 2003

File No.

Manager,
Industry #1
Commercial Services

Audit of bunker issues for vessels carrying bulk cargo for Assert Pty Ltd

As part of the recent audit of Assert Pty Ltd, an importer of bulk fertiliser, it was noted that their internal record keeping and document retention provided an auditable trail for bunker liability-sufficient to determine whether chartered vessels were or were not liable for bunkers. These records could not, however, determine whether bunkers were in fact paid, or the correctness of any amounts due.

Any amounts which were considered owing are of course the responsibility of the vessel owners, through the shipping company concerned, and as such, not the liability of the company being audited. Viewing of these records was by the clear consent and co-operation of Assert.

For the audit period, two vessels were noted from Assert records as exceeding the convention limit of 10% local cargo tonnage against vessel deadweight (see folios 1&2, 7&8). Tonnage and vessel status (domestic or international) at Australian ports of call was then confirmed against (database) records (folios 3&4, 10&11).

In both instances, the Ataraxia V29 and the Arabella V10, it was determined that bunkers were liable for some part of their Australian visit. A check with Customs Port N revealed that Customs had prompted payment in that port for the Ataraxia, as per folio 6. In Port G, an unmanned port, Beaufort Shipping had volunteered bunkers as per folio 13.

COMMENT: Although no extra revenue could be obtained from this aspect of the audit, despite some early promise based upon incorrect information from Customs Melbourne (see folio12) , it was considered a worthwhile exercise, and one that could possibly be kept in mind if we do any other audits of importers of bulk cargo. Certainly, the Port G payment appears to have been the result of self assessment, prior to the mooted self assessment/audit regime suggested in the current bunkers working party.

P Brady
Compliance Auditor
Petmin

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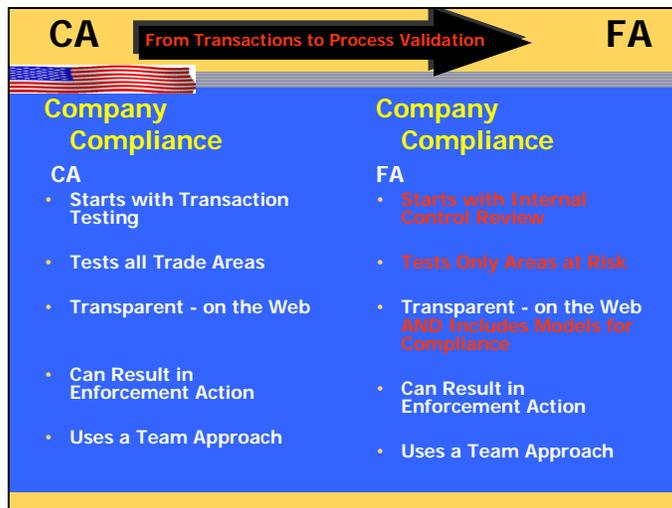
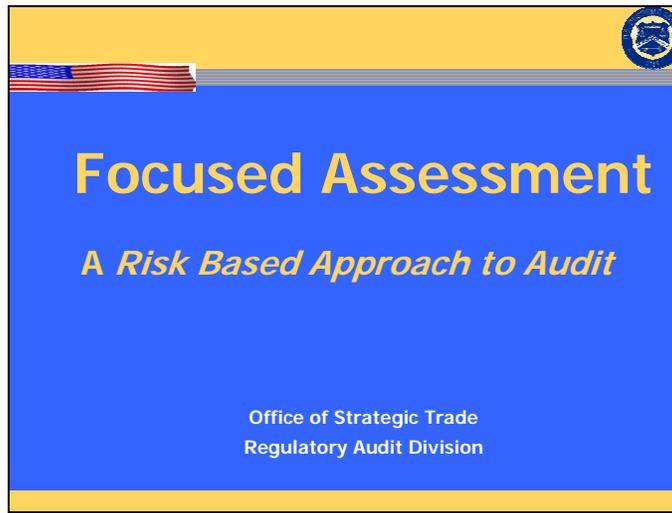
16 October 2003
Folder Of Attachments

ASSERT PTY LTD

Compliance Audit: Assert Pty Ltd (Division of DEEPCUT MINES Pty Ltd, July 2003)

<u>Attachment</u>	<u>topic covered</u>
1	????? report
2	T/A's issued & query reference
3	?????? data, DEEPCUT MINES
4	PWA's issued
5	Commodity queries from database extract
5A	Query data, Multi -K prills
6	obsolete tariff page for query 4 reference
7	?????? company data
8	listing of chemical synonyms & trade names
9	selection listing (initial) random & identified
10	database data, ship, o/ref dtar etc
11	database data invoice terms total, supplier etc
11A	Invoice totals, entered quantities
12	Company literature
13	Spreadsheet of shipping cargo/outturn data
14	Terminated entries

Appendix D3. USA Customs PowerPoint presentation on Focused Assessment.

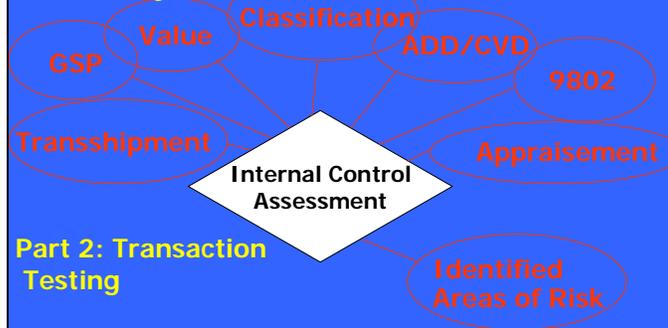


Focused Assessment Key Elements

- Starts with Internal Controls (Systems & Processes)
 - Good Internal Controls = Less Risk for Customs
- Evaluates Controls to:
 - Identify System Strengths & Weaknesses
 - Help Predict Future Compliance
- Zeroes in on Potential Material Risk
- Reduces Need for Extensive Transaction Testing
- Company Gets Blueprint for Future Compliance

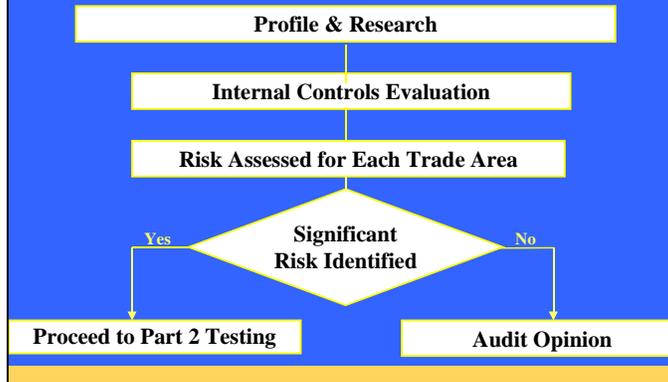
Focused Assessment - 2 Part Process

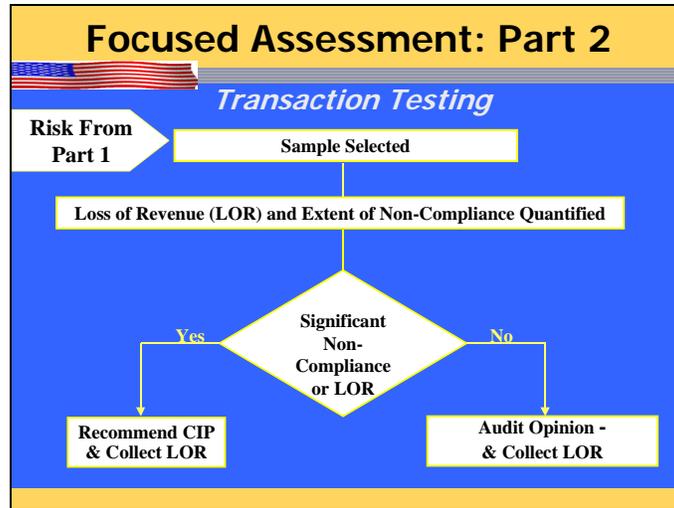
Part 1: Pre-Assessment Survey (PAS)



Focused Assessment: Part 1

Pre-Assessment Survey (PAS)





- ### Summary - The FA Process
- Consistent
 - Uses a Structured Approach
 - Transparent
 - On the Web
 - Provides Tools for Informed Compliance
 - Internal Control Model
 - Customs Best Practices
 - Statistical Sampling Based on \$ Value
 - Reflects Materiality
 - Company Blueprint for the Future

- ### What You Can Do
- Check our Web Site
 - Look for Strengths & Weaknesses in Internal Controls
 - Test Transactions When Weaknesses are Identified
 - Assess Your Risk of Non-Compliance

Example of PAS Results							
Elements Reviewed	PAS Internal Control Review					Results Significant Risk ?	Action Needed
	Company Profile	PAS Questionnaire	Process Review	Company Interviews	Limited Testing		
Value	PRI	PRI	RI	RI	RI	Yes	Stat. testing of royalties and assists to identify loss of revenue. Recommend CIP.
Classification	PRI	NRI	RI	RI	RI	Yes	Stat. testing of classification.
Quantity	PRI	NRI	PRI	NRI	NRI	No	No additional testing needed.
9801.00	PRI	NRI	RI	RI	RI	Yes	No additional testing needed. Company to quantify LOR and develop CIP.
9802.00.80	PRI	NRI	NRI	NRI	NRI	No	No additional testing needed.
AD/CVD	PRI	PRI	RI	RI	RI	Yes	No additional testing needed. Company to quantify LOR and develop CIP.
Legend:		<p>Summary Results: Six areas reviewed during Pre-Assessment Survey. Part two of the FA, Assessment Compliance Testing (ACT), will be required in only two areas. Four of the six areas reviewed had identified risks, however, either controls were satisfactory or remedies were identified that do not require additional Customs testing. The company agreed to quantify the loss of revenue and complete a CIP in two areas, 9801 and AD/CVD. Customs will follow up on their tests and conduct its own transaction tests on value and classification.</p>					
NRI – No risk indicated							
PRI – Potential risk indicated							
RI – Risk identified							

Appendix D4. USA Customs C-TPAT Validation Process Guidelines.

1.C-TPAT VALIDATION PROCESS GUIDELINES

I. Introduction

The Customs Service has developed a validation process to ensure that C-TPAT participants have implemented the security measures outlined in their Security Profile and in any supplemental information provided to Customs. The validation process will be conducted jointly by U.S. Customs personnel and a representative of the industry participant. The validation will focus on the material in the participant's C-TPAT security profile and any related materials provided by the participant and will be conducted under the guiding partnership principles of C-TPAT.

II. Objective

The purpose of the validation is to ensure that the supply chain security measures contained in the C-TPAT participant's security profile have been implemented and are being followed. In the context of the company's operations and the C-TPAT security recommendations, the validation team will evaluate the status and effectiveness of key security measures in the participant's profile and make recommendations where appropriate.

III. Validation Principles

The guiding principle of the C-TPAT program is partnership. The C-TPAT program is voluntary and designed to share information that will protect the supply chain from being compromised by terrorists and terrorist organizations. The validation process will enable Customs and the C-TPAT participant to jointly review the participant's C-TPAT security profile to ensure that security actions in the profile are being effectively executed. Throughout the process there will also be the opportunity to discuss security issues and to share "best practices" with the ultimate goal of securing the international supply chain. C-TPAT validations are not audits. In addition, they will be focused, concise, and will last not longer than ten work days.

Based on the participant's C-TPAT security profile and the recommendations of the validation team, Headquarters will also oversee the specific security elements to be validated.

IV. Conducting a Validation

1/23/2003

2. A. Validation Selection Process

To ensure their accuracy, the security profiles of C-TPAT participants will be validated. The order in which a C-TPAT participant's profile will be selected for validation will be based on risk management principles. Validations may be initiated based on import volume, security related anomalies, strategic threat posed by geographic regions, or other risk related information. Alternatively, a validation may be performed as a matter of routine program oversight. Customs Headquarters will schedule a company's first validation within approximately three years of the company becoming a C-TPAT certified participant. Customs field offices will not initiate validations and unannounced validations will not be conducted. C-

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TPAT participants will be given thirty days advance written notice along with a request for any supporting documentation that is needed.

B. Partnership Validation Teams

A Partnership Validation Team (PVT), consisting of Customs Office of Field Operations personnel and a representative of the C-TPAT participant, will conduct the on-site C-TPAT validation.

Customs representatives on a PVT will be officers knowledgeable in supply chain security matters. Customs PVT members will receive supply chain security training to assist them in working with industry representatives to promote effective corporate supply chain security programs. Customs Headquarters will determine the Customs representatives for each PVT. All Customs PVT representatives will be personnel from the Office of Field Operations.

The Customs Partnership Validation Team Leader (assigned by Customs Headquarters) will be responsible for the team's reviewing the company's security profile, other security information provided by the company, and data and information retrievable from other sources to determine the focus of the validation. This will help ensure that the validation is effective and limited in duration.

C. Validation Venue

A validation is an on-site review of the participant's C-TPAT supply chain security profile. The actual site of the validation may vary depending on the aspect(s) of the participant's profile that the "C-TPAT Validation Team" will review. Under normal circumstances the validation will begin with a briefing of company officials at the domestic corporate office or facility of the C-TPAT participant. If additional data or information is required to validate a portion of a C-TPAT participant's supply chain domestically or overseas, the PVT leader will request approval of travel through the Director, C-TPAT, at Customs Headquarters.

D. Validation Procedures

Upon receiving direction from Headquarters, Customs PVT leader will provide the company with a written notification of the scheduled validation. The notice will be issued at least thirty days prior to the start of the validation and will include a request for supporting documentation or materials, if any. The PVT leader will also contact the C-TPAT participant to establish a single point of contact at the corporate level.

Each validation will be customized for the participant involved and focused on the company's C-TPAT security profile. Prior to the on-site validation, the Customs representatives on the PVT will review the participant's C-TPAT security profile, any supplemental information received from the company, and any Customs Headquarters instructions, to determine the extent and focus of the validation.

In preparation for the on-site validation, the validation team may also consider pertinent C-TPAT security recommendations. A complete set of recommendations is included as Attachment A below. These security recommendations are a reference tool for considering the sufficiency of specific aspects of a participant's C-TPAT security profile. It is understood that the recommendations are not mandatory and are not all-inclusive with respect to effective security practices.

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As noted earlier, to begin the validation, the PVT will meet with company officials to discuss the process. Upon completion of the validation, the PVT will again convene with company officers to discuss validation findings. Although not a part of the PVT, the company's Customs account manager will normally attend the company briefings that initiate and complete the validation process.

E. Validation Report

Validation findings will be documented, included in the team's final report, and forwarded to the Director of C-TPAT for final editing and sharing with the C-TPAT participant. Ideally the report will affirm or increase the level of benefits provided to the participant. However, depending on the findings, some or all of the participant's C-TPAT benefits may be deferred until corrective action is taken to address identified vulnerabilities. With respect to actions resulting from a validation, Customs authority will rest with the Executive Director, Border Security and Facilitation.

ATTACHMENT A

PREFACE

The following outlines the C-TPAT Security Recommendations that may be used by the C-TPAT Validation Team in the planning phase of an on-site validation.

The recommendations are not mandatory for C-TPAT participation, but they may be helpful in the pre-validation review of key aspects of a participant's C-TPAT security profile. Therefore, prior to conducting an on-site validation, the validation team may review and discuss appropriate security recommendations contained in these attachments in the context of the participant's C-TPAT security profile. This will assist the team in limiting the scope of the validation and in customizing the validation to the C-TPAT participant involved.

1/23203

IMPORTERS

Develop and implement a sound plan to enhance security procedures throughout your supply chain. Where an importer does not control a facility, conveyance or process subject to these recommendations, the importer agrees to make every reasonable effort to secure compliance by the responsible party. The following are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Procedural Security: Procedures should be in place to protect against unmanifested material being introduced into the supply chain. Security controls should include the supervised introduction/removal of cargo, the proper marking, weighing, counting and documenting of cargo/cargo equipment verified against manifest documents, the detecting/reporting of shortages/overages, and procedures for verifying seals on containers, trailers, and railcars. The movement of incoming/outgoing goods should be monitored. Random, unannounced security assessments of areas in your company's control within the supply chain should be conducted. Procedures for notifying Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected, or suspected, by the company should also be in place.

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Physical Security: All buildings and rail yards should be constructed of materials, which resist unlawful entry and protect against outside intrusion. Physical security should include perimeter fences, locking devices on external and internal doors, windows, gates and fences, adequate lighting inside and outside the facility, and the segregation and marking of international, domestic, high-value, and dangerous goods cargo within the warehouse by a safe, caged or otherwise fenced-in area.

Access Controls: Unauthorized access to facilities and conveyances should be prohibited. Controls should include positive identification all employees, visitors, and vendors. Procedures should also include challenging unauthorized/unidentified persons.

Personnel Security: Companies should conduct employment screening and interviewing of prospective employees to include periodic background checks and application verifications.

Education and Training Awareness: A security awareness program should be provided to employees including the recognition of internal conspiracies, maintaining cargo integrity, and determining and addressing unauthorized access. These programs should offer incentives for active employee participation in security controls.

Manifest Procedures: Companies should ensure that manifests are complete, legible, accurate, and submitted in a timely manner to Customs.

Conveyance Security: Conveyance integrity should be maintained to protect against the introduction of unauthorized personnel and material. Security should include the physical search of all readily accessible areas, the securing of internal/external compartments and panels, and procedures for reporting cases in which unauthorized personnel, unmanifested materials, or signs of tampering, are discovered.

BROKERS

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Procedural Security: Companies should notify Customs and other law enforcement agencies whenever anomalies or illegal activities related to security issues are detected or suspected.

Documentation Processing: Brokers should make their best efforts to ensure that all information provided by the importer/exporter, freight forwarder, etc., and used in the clearing of merchandise/cargo, is legible and protected against the exchange, loss or introduction of erroneous information. Documentation controls should include, where applicable, procedures for:

- . Maintaining the accuracy of information received, including the shipper and consignee name and address, first and second notify parties, description, weight, quantity, and unit of measure (i.e. boxes, cartons, etc.) of the cargo being cleared.

- . Recording, reporting, and/or investigating shortages and overages of merchandise/cargo.

- . Safeguarding computer access and information.

Personnel Security: Consistent with federal, state, and local regulations and statutes, companies should establish an internal process to screen prospective employees, and verify employment applications. Such an internal process could include background checks and other tests depending on the particular employee function involved.

Education and Training Awareness: A security awareness program should include notification being provided to Customs and other law enforcement agencies whenever

Audit Training and Capacity Building

anomalies or illegal activities related to security are detected or suspected. These programs should provide:

- . Recognition for active employee participation in security controls.
- . Training in documentation fraud and computer security controls.

MANUFACTURERS

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case by case basis depending on the company's size and structure and may not be applicable to all. The company should have a written security procedure plan in place that addresses the following:

Physical Security: All buildings should be constructed of materials, which resist unlawful entry and protect against outside intrusion. Physical security should include:

- . Adequate locking devices for external and internal doors, windows, gates, and fences.
- . Segregation and marking of international, domestic, high-value, and dangerous goods cargo within the warehouse by a safe, caged, or otherwise fenced-in area.
- . Adequate lighting provided inside and outside the facility to include parking areas.
- . Separate parking area for private vehicles separate from the shipping, loading dock, and cargo areas.
- . Having internal/external communications systems in place to contact internal security personnel or local law enforcement police.

Access Controls: Unauthorized access to the shipping, loading dock and cargo areas should be prohibited. Controls should include:

- . The positive identification of all employees, visitors and vendors.
- . Procedures for challenging unauthorized/unidentified persons.

Procedural Security: Measures for the handling of incoming and outgoing goods should include the protection against the introduction, exchange, or loss of any legal or illegal material. Security

controls should include:

- . Having a designated security officer to supervise the introduction/removal of cargo.
- . Properly marked, weighed, counted, and documented products.
- . Procedures for verifying seals on containers, trailers, and railcars.
- . Procedures for detecting and reporting shortages and overages.
- . Procedures for tracking the timely movement of incoming and outgoing goods.
- . Proper storage of empty and full containers to prevent unauthorized access.
- . Procedures to notify Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected or suspected by the company.

Personnel Security: Companies should conduct employment screening and interviewing of prospective employees to include periodic background checks and application verifications.

Education and Training Awareness: A security awareness program should be provided to employees including recognizing internal conspiracies, maintaining product integrity, and determining and addressing unauthorized access. These programs should encourage active employee participation in security controls.

WAREHOUSES

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all. Warehouses as defined in this guideline are facilities that are used to store and stage both Customs

Audit Training and Capacity Building

bonded and non-bonded cargo. The company should have a written security procedure plan in place addressing the following:

Physical Security: All buildings should be constructed of materials, which resist unlawful entry and protect against outside intrusion. Physical security should include:

- . Adequate locking devices for external and internal doors, windows, gates and fences.

- . Adequate lighting provided inside and outside the facility to include parking areas.

- . Segregation and marking of international, domestic, high-value, and dangerous goods cargo within the warehouse by a safe, caged, or otherwise fenced-in area.

- . Separate parking area for private vehicles separate from the shipping, loading dock, and cargo areas.

- . Having internal/external communications systems in place to contact internal security personnel or local law enforcement police.

Access Controls: Unauthorized access to facilities should be prohibited. Controls should include:

- . The positive identification of all employees, visitors, and vendors.

- . Procedures for challenging unauthorized/unidentified persons.

Procedural Security: Procedures should be in place to protect against unmanifested material being introduced into the warehouse. Security controls should include:

- . Having a designated security officer to supervise the introduction/removal of cargo.

- . Properly marked, weighed, counted, and documented cargo/cargo equipment verified against manifest documents.

- . Procedures for verifying seal on containers, trailers, and railcars.

- . Procedures for detecting and reporting shortages and overages.

- . Procedures to notify Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected or suspected by the company.

- . Proper storage of empty and full containers to prevent unauthorized access.

Personnel Security: Companies should conduct employment screening and interviewing of prospective employees to include periodic background checks and application verifications.

Education and Training Awareness: A security awareness program should be provided to employees including recognizing internal conspiracies, maintaining cargo integrity, and determining and addressing unauthorized access. These programs should encourage active employee participation in security controls.

AIR CARRIERS

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Conveyance Security: Aircraft integrity should be maintained to protect against the introduction of unauthorized personnel and material. Conveyance security procedures should include the physical search of all readily accessible areas, securing all internal/external compartments and panels, and reporting cases in which unmanifested materials, or signs of tampering, are discovered.

Access Controls: Unauthorized access to the aircraft should be prohibited. Controls should include the positive identification of all employees, visitors and vendors as well as procedures for challenging unauthorized/unidentified persons.

Procedural Security: Procedures should be in place to protect against unmanifested material being introduced aboard the aircraft. Security controls should include complete, accurate and advanced lists of international passengers, crews, and cargo,

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as well as a positive baggage match identification system providing for the constant security of all baggage. All cargo/cargo equipment should be properly marked, weighed, counted, and documented under the supervision of a designated security officer. There should be procedures for recording, reporting, and/or investigating shortages and overages, and procedures to notify Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected or suspected by the carrier.

Manifest Procedures: Companies should ensure that manifests are complete, legible, accurate, and submitted in a timely manner to Customs.

Personnel Security: Employment screening, application verifications, the interviewing of prospective employees and periodic background checks should be conducted.

Education and Training Awareness: A security awareness program should be provided to employees including recognizing internal conspiracies, maintaining cargo integrity, and determining and addressing unauthorized access. These programs should encourage active employee participation in security controls.

Physical Security: Carrier's buildings, warehouses, and on & off ramp facilities should be constructed of materials which resist unlawful entry and protect against outside intrusion. Physical security should include adequate locking devices for external and internal doors, windows, gates and fences. Perimeter fencing should also be provided, as well as adequate lighting inside and outside the facility; including parking areas. There should also be segregation and marking of international, domestic, high-value, and dangerous goods cargo within the warehouse by means of a safe, cage, or otherwise fenced-in area.

SEA CARRIERS

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Conveyance Security: Vessel integrity should be maintained to protect against the introduction of unauthorized personnel and material. Conveyance security should include the physical search of all readily accessible areas, the securing all internal/external compartments and panels as appropriate, and procedures for reporting cases in which unmanifested materials, or signs of tampering, are discovered.

Access Controls: Unauthorized access to the vessel should be prohibited. Controls should include the positive identification of all employees, visitors, and vendors. Procedures for challenging unauthorized/unidentified persons should be in place.

Procedural Security: Procedures should be in place to protect against unmanifested material being introduced aboard the vessel. Security procedures should provide for complete, accurate and advanced lists of crews and passengers. Cargo should be loaded and discharged in a secure manner under supervision of a designated security representative and shortages/overages should be reported appropriately. There should also be procedures for notifying Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected, or suspected, by the company.

Manifest Procedures: Manifests should be complete, legible, accurate and submitted in a timely manner pursuant to Customs regulations.

Personnel Security: Employment screening, application verifications, the interviewing of prospective employees and periodic background checks should be conducted.

Education and Training Awareness: A security awareness program should be provided to employees including recognizing internal conspiracies, maintaining cargo integrity, and determining and addressing unauthorized access. These programs should encourage active employee participation in security controls.

Physical Security: Carrier's buildings should be constructed of materials, which resist unlawful entry and protect against outside intrusion. Physical security should include adequate perimeter fencing, lighting inside and outside the facility, and locking devices on external and internal doors, windows, gates, and fences.

LAND CARRIERS

Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Conveyance Security: Integrity should be maintained to protect against the introduction of unauthorized personnel and material. Conveyance security procedures should include the physical search of all readily accessible areas, securing all internal/external compartments and panels, and procedures for reporting cases in which unmanifested materials, or signs of tampering, are discovered.

Physical Security: All carrier buildings and rail yards should be constructed of materials, which resist unlawful entry and protect against outside intrusion. Physical security should include adequate locking devices on external and internal doors, windows, gates and fences. Perimeter fencing should be addressed, as well as adequate lighting inside and outside the facility, to include the parking areas. There should be segregation and marking of international, domestic, high-value, and dangerous goods cargo within the warehouse by a safe, caged or otherwise fenced-in area.

Access Controls: Unauthorized access to facilities and conveyances should be prohibited. Controls should include the positive identification of all employees, visitors, and vendors as well as procedures for challenging unauthorized/unidentified persons.

Procedural Security: Procedures should be in place to protect against unmanifested material being introduced aboard the conveyance. Security controls should include the proper marking, weighing, counting, and documenting of cargo/cargo equipment under the supervision of a designated security representative. Procedures should be in place for verifying seals on containers, trailers, and railcars, and a system for detecting and reporting shortages and overages. The timely movement of incoming and outgoing goods should be tracked and there should be procedures for notifying Customs and other law enforcement agencies in cases where anomalies or illegal activities are detected or suspected by the company.

Manifest Procedures: Companies should ensure that manifests are complete, legible, accurate, and submitted in a timely manner to Customs.

Personnel Security: Companies should conduct employment screening and interviewing of prospective employees to include periodic background checks and application verifications.

Education and Training Awareness: A security awareness program should be provided to employees including recognizing internal conspiracies, maintaining cargo integrity, and determining and addressing unauthorized access. These programs should encourage active employee participation in security controls.

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Develop and implement a sound plan to enhance security procedures. These are general recommendations that should be followed on a case-by-case basis depending on the company's size and structure and may not be applicable to all.

Procedural Security: Companies should notify Customs and other law enforcement agencies whenever anomalies or illegal activities related to security issues are detected or suspected.

Documentation Processing: Consolidators should make their best efforts to ensure that all information provided by the importer/exporter, freight forwarder, etc., and used in the clearing of merchandise/cargo, is legible and protected against the exchange, loss or introduction of erroneous information. Documentation controls should include, where applicable, procedures for:

- . Maintaining the accuracy of information received, including the shipper and consignee name and address, first and second notify parties, description, weight, quantity, and unit of measure (i.e. boxes, cartons, etc.) of the cargo being cleared.

- . Recording, reporting, and/or investigating shortages and overages of merchandise/cargo.

- . Tracking the movement of incoming and outgoing cargo.

- . Safeguarding computer access and information.

Companies should participate in the Automated Manifested System (AMS) and all data submissions should be complete, legible, accurate and submitted in a timely manner pursuant to Customs regulations.

Personnel Security: Consistent with federal, state, and local regulations and statutes, companies should establish an internal process to screen prospective employees, and verify applications. Such an internal process could include background checks and other tests depending on the particular employee function involved.

Education and Training Awareness: A security awareness program should include notification being provided to Customs and other law enforcement agencies whenever anomalies or illegal activities related to security are detected or suspected. These programs should provide:

- . Recognition for active employee participation in security controls.

- . Training in documentation fraud and computer security controls.

Appendix D5. “Using Excel as an Audit Software” by Richard B. Lanza.

This content was specifically designed for use and free distribution on

A community of professionals helping you to maximize the benefits of audit software

Using Excel as an Audit Software

By Richard B. Lanza, CPA, PMP

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Document Purpose / Call for Feedback

The purpose of this document is to assist auditors, fraud examiners, and management in implementing data analysis routines using Microsoft Excel. It is hoped that through the dissemination of this new information that more analysis will be done using audit software to prevent and proactively detect organizational inefficiency, ineffectiveness, and fraud. Please note that although written for auditors, these tests may greatly assist the business community at large as it is currently estimated that there are 400 million users worldwide.

This document is not expected to explain Microsoft Excel concepts at length but rather to provide guidance as to which of the product's features can be used in an audit setting. For more extensive documentation on the use of Microsoft Excel, please see the Help feature in the product and/or the publications section of the www.microsoft.com website. Another great site, using Excel from a financial perspective, is Business Finance Magazine's area on the use of Excel available at:

<http://www.bfmag.com/channels/BrowseArticles.cfm?TopicID=607&CurrChannel=0>

With this document, users can no longer say that audit software is difficult. For now, even a tool as simple as a spreadsheet can and should be used as an audit software. Many readers have noted that this document showed them what is possible with audit software in analogous terms they could understand.

With the "curtain exposed" users can now focus their time on the more critical activities of creatively dreaming up new tests and improving their business intelligence. For more information on the use of audit software, and countless ways of applying it to your business, please see www.auditsoftware.net/community/

If you would like to provide feedback on the document, we welcome and encourage it as we plan to complete later versions. Please provide your feedback via Email at questions@auditsoftware.net

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Limitations of Excel as an Audit Software

Although Microsoft Excel has many powerful features and can take on many of the features of an audit software, it has its own set of limitations that are presented below:

- . Can only process 65,536 rows or records of data which may be too small for most organizational databases. Please note however that many report writers (which can handle larger data sets) can define a smaller subset of data for further processing in Excel such as a particular company's division.

- . Does not document the auditor's work in easy to access logs for later reference and workpaper storage

- . Allows data to be changed in the spreadsheet

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. Can only read a small subset of the complete types of data files available in digital format. For example, EBCDIC files stored in IBM mainframes would need to be converted for use in Excel.

. Has difficulty in performing data management tests such as relating tables. Although it can be accomplished, it is an onerous task.

. Does not have functionality specifically tailored to the auditor. For example, a sample can be calculated in just a couple of clicks with minimal training in a specifically designed audit software. In Excel, it can be done, but it does take some effort and guidance.

. Does not easily apply routines from one data file to other data files whereas audit software can more easily “batch” audit routines for later use on the same file or different data files.

Therefore, for the above features, users should consider more specialized audit software such as ACL Software (www.acl.com) or IDEA Software (www.caseware.com). Otherwise, you could consider other database management software such as Microsoft SQL Server (www.microsoft.com) or Oracle (www.oracle.com). Another option is to review business intelligence tools such as COGNOS (www.cognos.com), Brio (www.brio.com) or Business Objects (www.businessobjects.com).

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Audit Software Tests

There are two types of audit software tests, those that are analytical in nature and those that are focused on applying analysis to the actual detailed data that are explained below:

1. Analytical Tests

Analytical Tests - evaluations of financial information made by a study of plausible relationships among both financial and non-financial data to assess whether account balances appear reasonable (AICPA, SAS 56)

This publication explains 11 analytical tests as follows

1. Horizontal Analysis
2. Vertical Analysis
3. Ratios
4. Trend Analysis
5. Performance Measures
6. Statistics
7. Stratifications
8. Aging
9. Benford’s Law
10. Regression
11. Monte Carlo Simulation

1.1 Horizontal Analysis

Analyzes the increases and decreases in a given balance, normally financial statement items, over two or more periods. This can be completed for the following information using the formula in the most righthand column (calculating column D):

- Balance sheet
- Income statement
- Budget to actual

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A B C D Formula

- 1 Asset Description This Year Last Year Difference
- 2 Cash \$1,000 900 (100) =**B2-C2**
- 3 Accounts Receivable 1,000 900 (100) =**B3-C3**
- 4 Fixed Assets 8,000 7,200 (800) =**B4-C4**
- 5 Total Assets **\$10,000 9,000** (1,000) =**B5-C5**

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1.2 Vertical Analysis

Examines the elements of a financial statement for a single period whereby each balance sheet item is shown as a percentage of the total assets and every income statement item is shown as a percentage of the net sales. This can be completed for the following balance sheet information using the formula in the most right-hand column (calculating column C):

A B C Formula

- 1 Asset Description Asset Balance % of Balance
- 2 Cash \$1,000 10% =**B2/B\$5**
- 3 Accounts Receivable 1,000 10% =**B3/B\$5**
- 4 Fixed Assets 8,000 80% =**B4/B\$5**
- 5 Total Assets **\$10,000 100%** =**B5/B\$5**

1.3 Ratios

One or more balances is compared with one or more other balances such as the relation of total assets to the net sales of an organization. Ratios can be organized into broad categories of “Liquidity/Debt” and “Profitability”.

The Excel calculations for the below ratio tests would be completed using formulas in Excel. For example, for the “Working Capital” (cell B4 below) ratio test, this may be completed as follows:

A B

- 1 Description Asset Balance
- 2 Current Assets \$1,000
- 3 Current Liabilities 800
- 4 Working Capital 200

Formula =B2-B3

A list of common ratio tests are listed below:

Liquidity/Debt – used to measure a company’s ability to pay its vendors or debt obligations in a timely manner.

Name Description

Working Capital (Current Assets - Current Liabilities)

Working capital index Current year WC - Prior year WC

Current Ratio (Current Assets / Current Liabilities)

Days Payable Outstanding (365 / (Sales / ((Beginning Accounts Payable + Ending Accounts Payable)/2)))

Days Sales Outstanding (365 / (Sales / ((Beginning Accounts Receivable + Ending Accounts Receivable)/2)))

Inventory turnover (Cost of Goods Sold / ((Beginning Inventory + Ending Inventory)/2))

Debt to Equity Total Debt / Total Stockholders Equity

Operating Cash Flow (Cash Flow From Operations / Current Liabilities)

Cash Flow Interest Coverage ((Cash Flow From Operations + Interest Paid + Taxes

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Paid) / Interest Paid)

Cash Flow to Capital Expenses Cash Flow From Operations / Capital Expenses

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Cash Flow to Debt Cash Flow From Operations / Total Debt

Obsolete Inventory Ratio Obsolete Inventory / Ending Inventory

Profitability – indicate the success of the organization in earning a net return on sales or on an investment.

Name Description

Sales growth index (Current Year Sales / Prior Year Sales)

Gross profit (Sales – Cost of Goods Sold)

Gross margin (Sales – Cost of Goods Sold) / Sales

Gross margin index (Current year Gross Margin / Prior year Gross Margin)

Stock sales (Ending Inventory / Sales)

Return on Equity (Net Income / ((Beginning Stockholders Equity + Ending Stockholders Equity)/2))

1.4 Trend analysis

Comparing any of the analytical tests (horizontal, vertical, ratio, etc.) described above over two or more periods. Please note that the use of trend analysis is practically a given in doing any audit work as fraud and errors tend to create variances over time which would go undetected if only the single year was being analyzed.

1.5 Performance Measures

The identification of critical success factors that can be tracked over time to assess progress made in achieving specific targets linked to an entity's vision. For example, the below represent a sampling of performance measures that could be used for accounts payable processing:

- Number of invoices processed
- Number of open invoices at period end
- Top 100 vendors purchases
- Average of top 25 max to min payments by vendor ratio
- % of adjustments to invoices processed
- Number of hours overtime worked by staff

The Excel calculations for the above performance measures would be completed using formulas in Excel (i.e., the Sum() function). For more discussion on Excel functions, please see the Extract/Filter section 2.5 of this document.

1.6 Statistics

Calculates various statistics. Regarding data such as average, high, low, standard deviation, etc. for a set of numbers. Statistics can be useful in determining the validity of data received and in completing highlevel trend analysis.

In order to calculate statistics in Excel, you will first need to add a piece of software that comes with the standard version of Excel. To use this add-in, go to the *Tools* menu in Excel and select *Add-Ins*. Then, Using Excel as an Audit Software

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when prompted, select the *Analysis Tool Pack* and press *OK*. This will add to the bottom of your *Tools* menu an item named *Data Analysis*.

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Once the information is input, select the *Data Analysis* menu item from the *Tools* menu. Then select the Analysis Tool *Descriptive Statistics* and press *OK* to view the *Descriptive Statistics Dialog Box*:

In the above example, an *Input Range* was entered and the results were pointed to a *New Workbook*. This produces the following results when the *OK* button is selected:

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1.7 Stratifications

Counts the number and dollar value of records of a population falling within specified intervals. Stratifications also provide a useful view into the largest, smallest, and average dollar transactions. An example stratification report by dollar amount is shown below:

Values

100

101

10

1,000

5,000

6,211 (total)

Stratification Report

Strata Count Dollars

0 to \$100 2 110

\$101to \$1,000 2 1,101

Over \$1,000 1 5,000

Total 5 6,211

To create the above Stratification Report, follow the two-step process below:

Step #1 – Complete a calculation of the strata using a multiple IF function in the right-hand column:

A B C

1 Value Strata (calculated

using formulas at

right)

Formula

2 100 1 =IF(A2>1000,"3",IF(A2>100,"2",IF(A2>0,"1","0")))

3 101 2 =IF(A3>1000,"3",IF(A3>100,"2",IF(A3>0,"1","0")))

4 10 1 =IF(A4>1000,"3",IF(A4>100,"2",IF(A4>0,"1","0")))

5 1,000 2 =IF(A5>1000,"3",IF(A5>100,"2",IF(A5>0,"1","0")))

6 5,000 3 =IF(A6>1000,"3",IF(A6>100,"2",IF(A6>0,"1","0")))

Please note that the above IF() function can only handle up to five multiple conditions shown above

and therefore, five strata for data stratification purposes.

Step #2 – Use the strata calculated above to populate the stratification table using the below COUNTIF ()

and SUMIF () formulas

Strata Strata Count Dollars

1 0 to \$100 =COUNTIF(B2:B6,1) =SUMIF(B2:B6,1)

2 \$101to \$1,000 =COUNTIF(B2:B6,2) =SUMIF(B2:B6,2)

3 Over \$1,000 =COUNTIF(B2:B6,3) =SUMIF(B2:B6,3)

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1.8 Aging

Produces aged summaries of data based on established cutoff dates. This is useful in understanding a process flow over time. An example aging report by dollar amount is shown below:

Strata Count Dollars
0-30 days 20 \$250
31-60 days 10 \$1500
Over 60 days 45 \$30,000
Total 75 \$31,750

The aging report uses the same concepts explained above for the Stratifications analytical test in section 1.7 of this document.

1.9 Benford's Law

Audit technology designed to find abnormal duplications of specific digits, digit combinations, specific numbers, and round numbers in corporate data. Since the objective is to find abnormal duplications, auditors need a benchmark that indicates a normal level of duplication. Benford's Law gives auditors the expected frequencies of the digits in tabulated data. The premise is that we would expect authentic and unmanipulated data to exhibit these patterns. If a data set does not follow these patterns, this may be a cause for auditor concern and to review those . The expected frequencies of Benford's Law for the first digits are:

Digit
First Digit
Frequency
0 -
1 0.30103
2 0.17609
3 0.12494
4 0.09691
5 0.07918
6 0.06695
7 0.05799
8 0.05115
9 0.04576

Step #1 - The first digits of any Excel field can be calculated as follows (using the formula in the righthand column):

A B
1 Values First Digit Formula for Column B
2 100 1 =LEFT(A2,1)
3 101 1 =LEFT(A3,1)
4 20 2 =LEFT(A4,1)
5 3,000 3 =LEFT(A5,1)

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6 5,000 5 =LEFT(A6,1)

Step #2 – Then use the results of the Left() formulas calculated above to populate the table using the below COUNTIF() function and a simple percentage formula:

D E F G
1 First Digit Count Percentage Benford's Law
2 1 =COUNTIF(B2:B6,1) =E2/E11 0.30103
3 2 =COUNTIF(B2:B6,2) =E3/E11 0.17609

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4 3 =COUNTIF(B2:B6,3) =E4/E11 0.12494
5 4 =COUNTIF(B2:B6,4) =E5/E11 0.09691
6 5 =COUNTIF(B2:B6,5) =E6/E11 0.07918
7 6 =COUNTIF(B2:B6,6) =E7/E11 0.06695
8 7 =COUNTIF(B2:B6,7) =E8/E11 0.05799
9 8 =COUNTIF(B2:B6,8) =E8/E11 0.05115
10 9 =COUNTIF(B2:B6,9) =E10/E11 0.04576
11 =Sum(E2:E10) =E11/E11

Large deviations between the calculated percentage (Column F) and Benford's Law (Column G) would be investigated. For more information on digital analysis and Benford's Law, please see the following article on ITAudit.org (<http://www.theiia.org/itaudit/index.cfm?fuseaction=forum&fid=95>).

1.10 Regression

Regression analysis calculates a dependent variable balance (i.e., net sales) based on various independent variables (i.e., product purchases, inventory levels, number of customers, etc.). Please note that this test generally provides the greatest level of precision because an explicit expectation is formed using all relevant data is incorporated into the model. It also provides a specific precision percentage for each test so that the auditor can assess the reliability of the test. Given the extensive nature of this topic, this document will not explain regression in depth. Instead, please see the following article which explains step-by-step how to use Excel to complete a regression analysis:

<http://www.auditsoftware.net/community/how/tool/tools/regexce.doc>

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1.11 Monte Carlo simulation

Monte Carlo allows for the simulation of a balance (i.e., net sales) using estimates where probabilities are given for each estimate. Please note that Monte Carlo simulates the balance estimate thousands of times to arrive at a final estimate with associated precision levels. To understand what Monte Carlo simulation does, think of flipping a coin one hundred times. More than likely, there will be close to 50 heads and 50 tails. Now, consider a revenue estimate model where there are best case, worst case, and most likely case scenarios given to the perceived market, the number of competitors, the price the market will bear, etc. In contrast with the simple coin flip, a highly advanced probability model can be developed in Monte Carlo tools. In other words, this allows you to flip ten differently weighted coins thousands of times to arrive at a final solution.

Given the extensive nature of this topic, this document will not explain Monte Carlo analysis in depth. For more information on Monte Carlo analysis, please see the following article which explains how add-on software can assist Microsoft Excel in easily calculating a Monte Carlo analysis:

<http://www.auditsoftware.net/community/how/tool/tools/Monte%20Carlo%20Article-Auditors.doc>

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2. Data Management/Analysis Reports

Data management/analysis reports are those that are run with common audit software yet many can be executed with database management software. These reports are further clarified with specific tests as explained in Chapter 5 of this document. Each type of report is briefly explained below:

Data Analysis Type Description

1. Append / Merge Combines two files with identical fields into a single file. An example would be to merge two years worth of accounts payable history into one file.
2. Calculated Field/Functions Created a calculated field (which can use a function such as ABS for the absolute value of the field) using data within the file. For example, the net payroll pay to an employee could be recalculated using the gross pay field and deducting any withholding/taxes.
3. Cross Tabulate Cross Tabulate lets you analyze character fields by setting them in rows and columns. By cross tabulating character fields, you can produce various summaries, explore areas of interest, and accumulate numeric fields.
4. Duplicates Identifies duplicate items within a specified field in a file. For example, this report could be used to identify duplicate billings of invoices within the sales file.
5. Extract/Filter Extracts specified items from one file and copies them to another file, normally using an “if” or “where” statement. Examples include extracting all balances over a predefined limit.
6. Export Creates a file in another software format (e.g., Excel, Word) for testing. An example would be to export customer address information to Word for “Mail Merge”ing to customer confirmation letters.
7. Gaps Identifies gaps within a specified field in a file. For example, identify any gaps in check sequence.
8. Index / Sort Sorts a file in ascending or descending order. An example would be sorting a file on social security number to see if any blank or “999999999” numbers exist.
9. Join / Relate Combines specified fields from two different files into a single file using key fields. This function is used to create relational databases on key fields. For example, the vendor masterfile could be related to the invoice file to obtain address information for each invoice.
10. Sample Creates random or monetary unit samples from a specified population.
11. Summarize Accumulates numerical values based on a specified key field. An example would be summarizing travel and entertainment expense amounts by employee to identify unusually high payment amounts.

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2.1 Append/Merge

Combines two files with identical fields into a single file. An example would be to merge two years worth of accounts payable history into one file as below:

Current Year File

A B C D E

1 Vendor Invoice Amount Check Check Date

2 11494 21597 13,466.25 6481 01/02/1996

3 1581600 29 3,562.50 6483 01/02/1996

+

Prior Year File

A B C D E

1 Vendor Invoice Amount Check Check Date

2 1564189 77976 48.48 6480 01/02/1996

3 25152 150842 72.56 6482 01/02/1996

4 25152 150684 566.02 6482 01/02/1996

Combined Current and Prior Year Files

A B C D E

1 Vendor Invoice Amount Check Check Date

2 11494 21597 13,466.25 6481 01/02/1996

3 1581600 29 3,562.50 6483 01/02/1996

4 1564189 77976 48.48 6480 01/02/1996

5 25152 150842 72.56 6482 01/02/1996

6 25152 150684 566.02 6482 01/02/1996

The Append/Merge in Excel is completed using a simple set of *Copy* and *Paste* commands found in the *Edit* menu. To complete, *Copy* range A1:E2 from the prior year file and *Paste* to a new sheet. Then *Copy* range A2:E3 from the current year file and *Paste* to the same new where the prior data was pasted.

This results in the “Combined Current and Prior Year Files” sheet with cells A1 to E6 of current and prior year data.

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2.2 Calculated Fields/Functions

Created a calculated field using data within the worksheet. For example, the net payroll pay to an employee could be recalculated using the gross pay field and deducting any withholding/taxes as below in column D:

A B C D Formula

1 Employee Gross Pay Tax & Other Net Pay For Column D

2 Mike \$1,000 300 700 =B2-C2

3 Jacob 1,000 280 720 =B3-C3

4 Denise 8,000 2,700 5,300 =B4-C4

5 **Total \$10,000 3,280 6,720 =B5-C5**

=SUM(B1:B4) =SUM(C1:C4) =SUM(D1:D4)

While the =SUM() function was utilized above, there are various other functions available in Excel.

Below are a sampling of the most common functions:

ABS() - Returns the absolute value of an expression (e.g., ABS(Check_Amount)

LOWER() – Converts a character field to all lower case.

LEFT() – Returns the left number of characters (as defined by the user) for the selected field.

LTRIM() - Removes all blank spaces from the left of a particular character field, moving all remaining characters to the left.

NPV() - Calculates the net present value of an investment by using a discount rate and a series of future payments (negative values) and income (positive values).

ROUND() – rounds a cell’s value to a specified number of digits.

SUM() – Adds the numbers in a range of cells.

UPPER() - Converts a character field to all upper case.

VALUE () - Converts a character expression or field into the numeric equivalent.

WEEKDAY() - Returns the day of the week corresponding to a date. The day is given as an integer, ranging from 1 (Sunday) to 7 (Saturday), by default.

WEEKNUM() - Returns a number that indicates where the week falls numerically within a year. Using Excel as an Audit Software

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2.3 Cross Tabulate

Cross Tabulate lets you analyze character fields by setting them in rows and columns. By cross tabulating character fields, you can produce various summaries, explore areas of interest, and accumulate numeric fields.

Excel effectuates cross-tabulation through its *Pivot Tables* feature explained below for the analysis of vendor payments in relation to approvers. To open the dialog box, select *Data* from the menu bar and *PivotTable and Pivot Chart Report...*:

The PivotTable Wizard will walk you through the selection of the data range and will result in the following dialog box:

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At this point, select the *Layout* button in order to establish the columns and rows of the pivot table. By starting with picture #1 below, the fields on the right (Approver, Vendor, and Amount) can be selected and dragged as shown in picture #2 below:

Please note that in the above box that the Sum of Amount field may start out as the Count of Amount when you first attempt this maneuver. To change it from Count to Sum (so that the total dollars can be calculated) drag it over and then double click on the Count of Amount. From here, simply change it to Sum. To close the Layout window, select OK and select Finish from the previous window.

Once complete, select the OK and then the Finish buttons to arrive at the below cross-tabulation:

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Please note that once this summary report is created, it can be filtered by the dropdown arrows (see above picture and section 2.6 of this document for more on Excel filters) so that purchases with a specific vendor could be summarized and reviewed in relation to the approvers of those purchases.

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2.4 Duplicates

Identifies duplicate items within a specified field in a file. For example, the below worksheet could be established to identify duplicate billings of invoices within the sales file where the same customer, invoice, and amount are the same:

A B C D

1 Invoice Customer Amount Duplicate

Y/N

Formula for Column D

2 77524 Sky's the Limit \$800.00

3 77525 Sky's the Limit \$1752.23 N =IF(AND(A3=A2,B3=B2,C3=C2),"Y","N")

4 77525 Sky's the Limit \$1752.23 Y =IF(AND(A4=A3,B4=B3,C4=C3),"Y","N")

5 77528 Sky's the Limit 922.00 N =IF(AND(A5=A4,B5=B4,C5=C4),"Y","N")

6 77535 Sky's the Limit 750.00 N =IF(AND(A6=A5,B6=B5,C6=C5),"Y","N")

Essentially, the *IF()* and *AND()* functions are used to create a column D which calculates whether the item is a duplicate.

Please note that the AND() function above can accept up to 30 expressions (three are used in the above

AND() function).

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2.5 Extract/Filter

Extracts specified items from one file and copies them to another file, normally using an “if” or “where” statement. Examples include extracting all balances over a predefined limit. This is most easily accomplished using the *Auto Filter* command under the *Filter* option of the *Data* menu.

For example, let's presume you needed to identify all payments to “Sky's the Limit Publishing” over \$1,000.

Step #1 – Highlight the row with each column's description (as the in below picture) and select the *Auto Filter* command under the *Filter* option of the *Data* menu (as the in above picture) to be presented with down arrows next to each column's description (as the in below picture):

Please note that in the above step that it is important there NOT be any clank lines between the column heading and the underlying data. Otherwise, the Filter will not operate effectively.

Step #2 – By selecting the down arrow next to the field **Vendor Name**, you will be presented with a list of all vendor names within that particular column. Using this, the “Sky's the Limit” vendor can be selected:

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This will filter all items in the worksheet with “Sky's the Limit” in the vendor name field. Then, the down arrow next to the **Invoice Amount** column can be selected and this time, the (*Custom...*) item can be selected (see above picture) to be presented with the following dialog box:

Working with the above box, the *is greater than* option can be selected and an amount *1000* can be entered to filter the invoice amount field for anything greater than \$1,000 where “Sky's the Limit” is the vendor, resulting in the below:

Please Note the following when using the *Auto Filter* feature in Excel:

. Using the (*Custom...*) feature, you can select up to three expressions with *AND* or *OR* statements in between each expression.

. Do not have any rows between the description row and the data or the *Auto Filter* feature will not operate properly.

. Do not have any blank rows within the worksheet data or the *Auto Filter* feature will not operate properly.

. To remove the *Auto Filter* feature, select *Auto Filter* command under the *Filter* option of the *Data* menu which will deselect the command.

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2.6 Export

Creates a file in another software format for testing. An example would be to export customer address information to a tab delimited file so that it may be imported within another audit software. All exporting from Excel is effectuated through the *Save As* feature in the *File* menu. Common options for exporting data include:

- . Comma delimited
- . Dbase
- . Tab delimited
- . Web page

2.7 Gaps

Identifies gaps within a specified field in a file. For example, to identify any gaps in check sequence in the below table, the following formula (see cell C3) would be entered and copied down for the entire length of data in the worksheet (in this spreadsheet this would start at B3 and copied down to B6):

A B C

1 Check Number Gaps Formula for Column B

2 77524 0

3 77525 0 =IF(A3-A2<>1,(A3-A2)-1,0)

4 77527 1 =IF(A4-A3<>1,(A4-A3)-1,0)

5 77528 0 =IF(A5-A4<>1,(A5-A4)-1,0)

6 77535 6 =IF(A6-A5<>1,(A6-A5)-1,0)

*****Please note that before you run the GAPS test above, you need to sort your file on the field being**

tested for gaps in Ascending order (see 2.8 Index/Sort Below)

2.8 Index / Sort

Sorts a file in ascending or descending order. An example would be sorting a file on social security number to see if any blank or “999999999” numbers exist. To sort a file in Excel, the range of data must first be highlighted. Then, the *Sort* command is selected from the *Data* menu item to be presented the following self-explanatory dialog box:

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2.9 Join / Relate

Combines specified fields from two different files into a single file using key fields. This function is used to create relational databases on key fields and mainly uses the *VLOOKUP()* function in Excel. Please note that of all of the Excel uses as an audit tool, the joining of files is most difficult and better completed by an audit or database software. However, simple joining of files is possible and explained further below.

For example, to join the vendor masterfile to the employee masterfile on the address column, the following functions (column E and G) need to be defined (which are further explained below the picture):

Step 1: Join the vendor and employee address columns using the formulas listed in column D. The *VLOOKUP()* function takes an address in column C (employee address) and matches it to Column A

(vendor address). Please note that Excel looks for the most precise value and will not leave the calculated column blank. Therefore,

A B C D

1

2

3

Vendor Address Employee Address

Most Likely Vendor

Address Formula for Column D

4 120 Berger Place 20816 HardwoodCourt 145 Ridge Road
=VLOOKUP(C4,A\$3:A\$8,1)

5 145 Ridge Road 22 Waverly Place 22 Waverly Place =VLOOKUP(C5,A\$3:A\$8,1)

6 22 Waverly Place 35 Waldorf Avenue 2412 Maple Ave
=VLOOKUP(C6,A\$3:A\$8,1)

7 2300 Pilgrim Lane 4 Meadowland Court 2412 Maple Ave
=VLOOKUP(C7,A\$3:A\$8,1)

8 2412 Maple Ave 42 Park Avenue 2412 Maple Ave =VLOOKUP(C8,A\$3:A\$8,1)

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Step 2: Now that the most likely vendor address matching to the employee address has been calculated, a simple IF() function is written to identify any true matches between the vendor and employee address files.

Match? Formula

N =IF(D4=C4,"Y","N")

Y =IF(D5=C5,"Y","N")

N =IF(D6=D6,"Y","N")

N =IF(D7=D7,"Y","N")

N =IF(D8=D8,"Y","N")

The end result in the above analysis is that cell C3 (Waverly Place) has a match between the vendor and employee address files which is noted with a “Y” in the above picture.

Key Note on Joining Files Using VLOOKUP: Please note that matching on an entire address field, as in the above example, may not be practical given address fields in the vendor and employee masterfile may be entered differently. For example “123 Maple Street” in the vendor file may be “123 Maple St.” in the employee file and therefore not show up as a match.

To avoid the above problem, the LEFT() function may be used to select say the first 8 characters of the address fields. For example, LEFT(A4,8) in the above example would return “123 Berg”. This calculated field could be made for both the vendor and employee address columns and a VLOOKUP used on the newly calculated column to get a match on the first eight characters of the address field.

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2.10 Sample

Creates random or monetary unit samples from a specified population. In Excel, a random sample can be easily completed as follows for a sampling of data below:

Step #1 - In order to calculate statistics in Excel, you will first need to add a piece of software that comes with the standard version of Excel. To use this add-in, go to the *Tools* menu in Excel and select *Add-Ins*.

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Then, when prompted, select the *Analysis Tool Pack* and press *OK*. This will add to the bottom of your

Tools menu an item named *Data Analysis*.

Step #2 – Select the *Random Number Generator* option as seen below:

Step #3 – Complete the resulting dialog box noting the following:

. The *Number of Random Numbers* should equate to the number of rows in the file. In my example (below picture) there are fifteen items in the row.

. The *Distribution* should be set to *Uniform*.

. A *Random Seed* should be entered which will affect the generation of random numbers. It is suggested that a different seed number be entered for each sample selected.

. An *Output Range* must be designated which is suggested to be next to the data to be sampled as done in the below dialog box with the results seen on the following page.

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Step #4 – Once the random numbers have been generated and placed next to the data for sampling, the worksheet of data would need to be sorted using the *Sort* command in Excel (see section 2.8 of this document).

Final Result – With the final results sorted in ascending order (see below picture) a sample can be selected starting with the first item and working downwards. For example, if five items were to be sampled, the first five items would represent the random sample (see below picture):

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2.11 Summarize

Accumulates numerical values based on a specified key field.

For example one potential test could be summarizing travel and entertainment expense amounts by employee to identify unusually high payment amounts. To complete this test, first sort the data using the *Sort* command explained above. Then, highlight the data to subtotal and then select *Subtotals* from the *Data* menu item to be presented with the following dialog box:

Using this dialog box, the columns to subtotal can be selected and, when finished, the *OK* button can be selected to complete the summarizations below. Please note that Options 1, 2, and 3 relate to the button on the left-top side of each individual picture below to be presented with a grand total (Option 1), a total by employee (Option 2) or a detail listing with subtotals (Option 3):

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About the Author

Rich Lanza (CPA, PMP) is a Manager of Internal Audit at a Fortune 200 retailer, where he focuses mainly on using computer assisted audit tools to improve business intelligence, increase efficiencies, and identify multi-million dollar bottom-line savings.

Rich is a leading authority on the use of data extraction/analysis technology. He has devoted himself to freely providing information on the topic as his mission is to help auditors get recognized for their bottom-line results. To that end, he founded

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AuditSoftware.Net (www.auditsoftware.net/community) that works to increase organizational benefits from the use of audit software. The free site provides tools, case studies, a vendor discount program, newsletter, and a discussion area to visitors. The site recently announced project communities whereby anyone interested can share and collaborate on practical audit software tools and solutions. Rich has also written numerous articles, software products, and four test set books on how to practically apply ACL and IDEA software (<http://www.ekaros.ca/publications.html>). Rich headed the Program Management Office, reporting to the Chief Operating Officer at the American Institute of Certified Public Accountants, where he sewed a culture of project management into the fabric of the organization. On his last major project, Rich worked to coordinate various fraud-reduction initiatives to maximize their benefit for the AICPA and financial markets. Rich has drafted many of the project standards being used at the AICPA to manage projects and has implemented a project portfolio management process. He has also established a six-month intense training program for project managers.

Prior to his program management work, Rich was a program/project manager in many Web and technology projects including leading the Y2K project. Prior to joining the AICPA, Rich served as a Vice President-Audit Technology at AuditWatch where he was an *ACL*® and *IDEA*™ trainer. He has also been an Internal Audit Manager for Lafarge and Disclosure and has served in the audit department at KPMG Peat Marwick. Rich received his undergraduate degree in public accounting from Pace University. He is a past President of the Northern Virginia Chapter of The Institute of Internal Auditors, and is a certified member of both the AICPA and PMI. He currently also maintains the New York/New Jersey Program Management Office Special Interest Group for PMI. In 2003, for his data analysis work in the area of fraud detection, he was awarded the Outstanding Achievement in Commerce Award from the Association of Certified Fraud Examiners and in he won the Second Annual *ACL* Users Challenge. His interests include magic, and collecting gadgets. The author's opinions expressed in this publication are his own and do not necessarily represent the policies or positions of his employer.

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Appendix D6. Audit tasks table.

What Does Each Task Involve?

The following table provides details of the steps within each task as well as an overview of what each task and step aims to achieve.

<i>Tasks</i>	<i>Steps</i>	<i>Comments</i>
1 Preliminary activity and planning including systems description and verification	1.1 Obtain and evaluate background information available in-office and establish audit objectives, scope and focus.	Background information can be obtained from a number of sources, eg previous audit reports, mainframe systems etc. An initial audit plan is prepared based on information gathered to date.
	1.2 Conduct the entry interview.	The purpose of entry interview is to explain the purpose of the audit to the client, to address administrative matters and to discuss legislative requirements.
	1.3 Information gathering, systems description and verification.	During this step the auditor will gain information from the company about key personnel and company systems. The systems as they apply to Customs / Revenue needs are documented. The systems description should also be confirmed.
	1.4 Form an opinion upon the approach to be taken	A preliminary opinion can now be made whether to continue with a systems based approach or to adopt a transaction based approach.
2 Analytical checking and Initial Assessment	2.1 Conduct analytical checks	These checks compare relationships among financial and non-financial data. The results of these checks are considered in the next step.
	2.2 Make Initial Assessment.	The auditor now forms a preliminary opinion as to the level of confidence concerning the company's level of compliance. This opinion is based on all of the information collected to date and the results of analytical checks.

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<i>Tasks</i>	<i>Steps</i>	<i>Comments</i>
	2.3 Decide on approach to be taken	A decision may now be made whether to use a systems based or transactional approach.
3 Control identification and evaluation.	3.1 Identify potential errors	The auditor now identifies errors which could occur and which would result in reduced compliance with Customs / Revenue requirements.
	3.2 Identify controls	The auditor now identifies controls in the company systems which would prevent or detect the potential errors identified above.
	3.3 Evaluate controls	An evaluation is now made on the auditor's confidence level that the controls are sufficiently strong to prevent or detect the potential errors. Any controls which are needed and are missing should also be identified and recorded for later action.
	3.4 Complete final audit plan	A decision will now be made whether to use a systems based or transactional approach. A final audit plan is completed
4. Compliance testing and control assessment	4.1 Test controls	Checks are designed and conducted to determine whether the controls are being applied.
	4.2 Control assessment	An assessment is made on the effectiveness of the control environment based on the results of the checks.
5. Substantive testing (checking of records and transactions).	5.1 Design substantive tests	Checks of transactions are designed and conducted to verify that the client is satisfying Customs requirements.
	5.2 Conduct substantive tests.	
	5.3 Conclude on results	Results are assessed and conclusions made.
6. Treating issues from the audit	6.1 Address issues	All issues which arose during the audit are addressed.
	6.2 Resolve issues or follow up	Unresolved issues are followed up.
7. Audit reporting	7.1 Reports are completed	A report including working papers is completed for Customs / Revenue management. A report is completed for the client.

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<i>Tasks</i>	<i>Steps</i>	<i>Comments</i>
	7.2 Exit interview is conducted	An exit interview is conducted with the client.

Appendix D7. Modified CAPE matrix

Ref:

CAPE Matrix - Importers

Potential Errors	Internal Controls Identified (S=strong, W=weak)										Tests (C=compliance, S=substantive, O=observation)									
Invoice quantity <>																				
Customs Dec. qty.																				
Invoice value <>																				
Customs Dec. value																				
Incorrect C/O on Customs Dec.																				
Invoice desc. <> tariff item used																				
Agreements not satisfied																				
Exemptions incorrectly claimed																				
Incorrect trade marks																				
Inv. Qty. incorrect																				
Inv. Desc. Incorrect																				
Inv. Value incorrect																				

Internal controls described at reference:

Company:
Auditor:
Date:
Certified:

Tests described at reference:

**Appendix E1
Original Course Timetable**

Compliance Audit Techniques

Saturday 5 June – Thursday 17 June

Training hours

Saturday 5 June & Saturday 12 June – **0900 – 1500**

Wednesday 9 & Tuesday 15 0900 - 1300

All other days – **1300-1700**

Timetable

Day	Session	Content
Saturday 5 June	1	Administration & introduction
	2	Overview
	3	Overview
Sunday 6		Process mapping
Monday 7		Flow charting
Tuesday 8		Systems analysis
Wednesday 9		Field visit
Thursday 10		Analysis of field visit data
Saturday 12	1	Sampling
	2	Sampling
	3	Sampling
Sunday 13		Testing and assessments
Monday 14		Working papers
Tuesday 15		Field visit
Wednesday 16		Analysis of field visit data
Thursday 17		Reporting & review

Note: Each day after day one will begin with a review period to discuss issues arising from earlier sessions.

**Appendix E2
Revised Course Timetable**

Compliance Audit Techniques

Saturday 5 June – Thursday 17 June

Training hours

Saturday 5 June & Saturday 12 June – **0900 – 1500**

Wednesday 9 & Tuesday 15 0900 - 1300

All other days – **1315 - 1700**

Timetable

Day	Session	Content
Saturday 5 June	1	Administration & introduction
	2	Overview
	3	Overview
Sunday 6		Process mapping
Monday 7		Flow charting
Tuesday 8		Systems analysis
Wednesday 9		Field visit
Thursday 10		Analysis of field visit data / charting / CAPE matrix
Saturday 12	1	Sampling theory
	2	Sampling methodology
	3	CAPE matrix
Sunday 13		Extended review / audit process / working papers
Monday 14		Company analysis / testing
Tuesday 15		Field visit
Wednesday 16		Analysis & compilation of field visit data
Thursday 17		Reporting, team structure & review

Note: Each day after day one will begin with a review period to discuss issues arising from earlier sessions.

Appendix F

Australian Taxation Office brochure “If you're subject to enquiry or audit”

If you're subject to enquiry or audit

Who this is for

This information is for everyone who deals with us on tax matters, including superannuation, excise and the Higher Education Contribution Scheme. Unless we say otherwise, ‘tax’ means all matters dealt with by the Tax Office.

Enquiries or audits conducted by us vary in their level of complexity. Sometimes they only involve a phone call or a letter asking you to provide further information or verification of your claims. In some cases a tax officer may visit you.

The general principles under [‘What you can expect of us’](#) apply to all forms of enquiry or audit. However, most of the information in this booklet only applies to face-to-face enquiries and audits.

Not all face-to-face visits are the enquiries or audits this booklet covers. Some are just to provide assistance and information while others are routine checks of simple details you would normally have on hand, such as your Australian business number or GST registration. If a tax officer visits you, they’ll let you know the purpose of the visit at the outset.

Introduction

We presume that you are trying to deal honestly with your tax affairs.

We have a responsibility to the government and the community to try to ensure that everyone pays the correct amount of tax or receives the correct entitlement under the law. For this reason, we sometimes check the accuracy of information that you give us.

If we undertake checks of your tax affairs it doesn’t mean we think you’re dishonest. We accept that honest mistakes can be made. If you make an honest mistake, where allowed under the law, we take this into account when considering any penalties that may be imposed.

In addition to honest mistakes, the law recognises that errors can be caused by a range of factors including carelessness, recklessness or intentional disregard of the law.

If we discover that a taxpayer has intentionally sought to avoid paying tax or over-claimed payments, we take firmer action in considering penalties and possible prosecution action.

More information on [honesty](#)

The enquiry or audit process

An enquiry or audit usually involves examining your tax affairs to make sure that the information is accurate and to confirm your taxation liability or entitlement.

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We may also contact other parties such as banks, employers, customers and suppliers to obtain information.

What you can expect of us

We're required to conduct enquiries and audits in an impartial, fair, reasonable and professional manner. Regardless of the type of enquiry or audit, the following principles apply:

- we treat all taxpayers in accordance with the law and the principles outlined in the Charter
- the tax officer conducting the enquiry or audit will outline the audit process and, where appropriate, will endeavour to guide you through the process—particularly if you're experiencing an audit for the first time or you're not represented by a professional adviser, and
- we seek to minimise cost and inconvenience to you.

Our audits are subject to quality assurance checks to ensure that we act in accordance with these commitments.

What is expected of you during an enquiry or audit

We prefer an informal and cooperative approach when requesting information and obtaining access to premises, records (including electronic records) and documents. We seek your cooperation in doing this by:

- providing our officers with full and free access to buildings, premises, records and documents, other than those documents which may remain in confidence between you and your barrister, solicitor or professional accounting adviser
- allowing us to make copies of, or take extracts of, records and documents other than those which may remain in confidence between you and your barrister, solicitor or professional accounting adviser
- providing reasonable facilities and assistance to us
- providing complete and accurate responses to requests for information, and
- being truthful and honest in your dealings with us.

How to prepare for an enquiry or audit

If you've been notified of an enquiry or audit, you should prepare for it by reviewing your relevant records, tax returns and activity statements.

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Any error should be immediately brought to our attention. If you do this, the level of penalty that may otherwise have been imposed may be reduced.

If you notify us of any error before we notify you of an audit, the level of penalty that may otherwise have been imposed will be reduced.

Notification of an enquiry or audit

In most circumstances, you'll be notified of our intention to make enquiries or conduct an audit of your tax affairs. The notification will be in writing, normally be made to your address for service, and may be preceded by a phone call.

This notification will:

- tell you the name and telephone number of the tax officer conducting the enquiry or audit
- explain the expected nature, scope and duration of the enquiry or audit and indicate the information and records that will be required. We'll seek to complete the enquiry or audit in the shortest possible time, but the time it takes depends on several factors such as the type of enquiry, the adequacy of your records, the availability of information, the complexity of the matter and the level of your cooperation
- advise you that you may have a representative present at the start or at any stage of the enquiry or audit. If you need to consult with your representative, you'll be given reasonable time and opportunity to do so, and
- tell you about your rights and obligations in relation to the enquiry or audit.

There may be situations where we decide that urgent access action is appropriate and prior warning may not be given. For example, there may be a reasonable belief that the existence or integrity of documents, information or goods is under threat. Urgent access requires the approval of a senior tax officer. In these cases we'll give you reasonable time and opportunity to consult your representative after the urgent access.

At the start of the enquiry or audit

At the initial interview the tax officer conducting the enquiry or audit will:

- provide Tax Office identification and a telephone contact number when first meeting you (unless this has already been done), as will any other tax officers present
- if you ask, tell you the name and telephone number of their manager, except in very limited circumstances, and

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- give you the opportunity to volunteer information about any possible irregularity or omission in relation to your tax affairs. If you do this, the penalty that may otherwise have been imposed may be reduced.

During an enquiry or audit

We will:

- seek to arrange any interviews or meetings at times and places that are mutually convenient, usually during normal business hours
- explain the purpose of any interview or visit
- ask clear and unambiguous questions and provide you with all reasonable assistance and explanations to clarify their meaning
- allow you to choose someone to act on your behalf or to attend interviews with you
- inform you in advance when the tax officer will have a legal adviser present to assist them during an interview
- give you reasonable time to collect records, documents and papers for examination and to gather information about any matter that arises, unless we have reason to believe that the existence or integrity of the documents is at risk
- answer any reasonable and relevant questions you ask relating to the enquiry or audit
- allow you to take notes of any conversations or interviews
- if you ask, or where we consider it reasonable to do so, tape record interviews. A copy of the audio tape will be provided to you, free of charge, at the conclusion of the interview
- if you ask, provide you with a signed copy of the tax officer's written record of interview. If we ask you to sign the record of interview, we'll explain the implications of doing this
- respect your right, and give you adequate opportunity to claim, legal professional privilege in relation to certain communications between you and your barrister or solicitor

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- in certain circumstances, allow for some advice to remain in confidence between you and your professional accounting adviser. Further details on this and legal professional privilege are contained in the Tax Office's *Access and Information Gathering Manual*
- provide a written receipt for any records that we collect in person at an interview and return the records as soon as possible or as mutually agreed
- use discretion if and when we make any enquiries of third parties and do so without any implication of wrongdoing by you
- allow you the opportunity to give your views on any relevant issue, including any proposed adjustments, and
- keep you informed of the progress of the enquiry or audit. How often this happens will vary according to the type of enquiry or audit being conducted.

If you don't speak English, we'll arrange with you for an interpreter to attend any meetings or interviews. You can also request that telephone interviews are carried out through the Translating and Interpreting Service.

Interpreters can only interpret what you say. They can't answer questions for you unless you have authorised them to act on your behalf.

Formal powers

We prefer to adopt an informal and consultative approach when requesting information and obtaining access to premises and documents.

However, under the tax laws, the Commissioner can require a person to provide information, to attend and give evidence, or to produce any books, documents or other papers in the custody of or under the control of that person.

When you're required under the law to attend a formal interview, you are the person who must answer any questions asked in the interview.

You may still choose to have your representative or adviser present. In this situation, you'll be given a reasonable opportunity to consult with your representative or adviser who can only advise you as to the meaning of a question, not what answer you should give.

In very limited circumstances, you won't be allowed to have your representative or adviser present, such as when your representative or adviser may have had a role in the transaction under review. In this situation, you'll be given reasonable time to obtain alternative representation.

Should you be required under the law to attend a formal interview, the tax officer will provide you with an explanation, before the interview, that the law obliges you to answer questions put to you during the interview.

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If you bring an interpreter to a formal interview because you don't speak English, you're allowed to answer through the interpreter.

At the completion of an enquiry or audit (or, in some cases, during an enquiry or audit)

We will:

- clearly explain the basis of any adjustments made as a result of the enquiry or audit
- inform you if any error has been detected which has resulted in you paying too much tax or receiving less than your entitlement
- clearly explain the reasons for any penalty or interest and how this will be calculated
- give you the opportunity to explain any circumstances which you believe could justify a reduction of any penalty or interest
- provide you with written notification of the outcome of the enquiry or audit. We aim to do this within seven days of making our decision
- inform you of your review rights and the remedies that may be available to you, and
- draw to your attention any matters that will help you to understand and meet your taxation obligations in the future.

Settlement meetings are usually held for more involved or complex audits. If there is a settlement meeting (or the equivalent type of meeting in the case of excise duty collections or excise payments schemes matters):

- the tax officer conducting the audit will be accompanied by at least one other officer except in the most simple matters
- settlement agreements will be reached without any inducements or duress and will be undertaken in accordance with the *Code of Settlement Practice* which is available for inspection or purchase. For more information, talk to the tax officer conducting the audit or enquiry, or contact us, and

document the terms of any settlement agreement reached and provide you with a copy.

Penalties and offences

In conducting audits and making enquiries, we may determine that you have underpaid your tax or received more payment than you were entitled to.

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Generally, the tax laws provide for penalties to be imposed where the requirements of the law have not been met. Excise payment laws provide for penalties by way of a monetary amount. In both cases there are different rates of penalty based on the type of behaviour or the degree of culpability involved.

The law also provides for prosecution action to be undertaken for a range of taxation related offences. These offences include making a false or misleading statement in a tax return, making a false or misleading statement to a tax officer and keeping incorrect or false records with an intention to deceive or mislead a tax officer.

More information on [penalties and offences](#)

If you want to make a complaint

If you're dissatisfied with the way in which an enquiry or audit is being conducted, including if you are concerned about any apparent delays or the length of time involved in the process, you should raise your concerns with the tax officer you're dealing with.

If the issue can't be resolved, make your concern known to that officer's manager.

If you are still not satisfied, phone our complaints line on 13 28 70. You may be asked to put the complaint in writing.

You also have the right to make a complaint to the [Taxation Ombudsman](#). If you think your privacy has been breached, you have the right to make a complaint to the [Federal Privacy Commissioner](#).

More information about [making a complaint](#)

Complaints about the behaviour of a tax officer

If you wish to make a complaint about the behaviour of a tax officer, you should talk to that officer's manager. They will discuss the issue with you and try to resolve the matter informally. If you're not satisfied contact the Tax Office's complaints line on 13 28 70. You may be asked to put the complaint in writing.

In dealing with a complaint against a staff member, we are committed to providing fairness for both the complainant and the staff member involved. We take an objective, impartial and balanced approach and follow the principles of natural justice and procedural fairness for all parties.

More information

To order a printed copy of any of the [Taxpayers' Charter publications](#), phone our publications distribution service on 1300 720 092. For each booklet you order, please quote the full title and NAT number.

To discuss specific tax matters, refer phone [our helplines](#).

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